TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1931

No. 426

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

vs.

CHARLES P. LEININGER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR CERTIORARI FILED SEPTEMBER 30, 1931
CERTIORARI GRANTED NOVEMBER 2, 1931

SUPREME COURT OF THE UNITED STATES

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1 Before United States Board of Tax Appeals

Docket No. 15295

CHARLES P. LEININGER, 2231 CHATFIELD DRIVE, CLEVELAND, OHIO, Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For petitioner, Irwin N. Loeser, Esq.; for respondent, John D. Kiley, Esq.

Docket entries

1926
Apr. 29. Petition received and filed.
May 3. Copy of petition served on solicitor.
May 3. Notification of receipt mailed taxpayer.
June 1. Motion for 120 days extension to file answer filed by solicitor.
June 1. Granted. Both sides notified.
Oct. 30. Answer filed by general counsel.
Nov. 5. Copy of answer served on taxpayer. General calendar.
1928
June 29. Notice of hearing Oct. 4, 1928.
Sept. 11. Motion to place proceeding on the Cleveland, Ohio, circuit calendar and to consolidate for hearing with docket 23917, filed by taxpayer.
Sept. 28. Circuit hearing granted.
1929
Apr. 18. Notice of the appearance of Irwin N. Loeser, attorney for taxpayer.
May 9. Hearing set 6-4-29 at Cleveland, Ohio.
June 4. Hearing had before Ernest H. Van Fossan, Div. 9, on merits. Petitioner's motion for judgment held C. A. V. Consolidated with 23917. Stipulation by counsel read into record. Briefs due 60 days—Aug. 3, 1929.
July 11. Motion for extension of time to Oct. 1, 1929, to file brief filed by general counsel. 7-12-29 granted.
July 15. Transcript of hearing June 4, 1929, at Cleveland, Ohio, filed.
Aug. 3. Brief filed by taxpayer.
Sept. 27. Brief filed by general counsel.
2 1930
Apr. 16. Findings of fact and opinion rendered, E. H. Van Fossan, division 9. Judgment will be entered for respondent.
Apr. 19. Decision entered. E. H. Van Fossan, division 9.
Apr. 24. Petition for reargument and rehearing filed by taxpayer.
May 8. Order denying motion for rehearing entered.
June 10. Supersedeas bond for $18,500 approved and ordered filed.
June 10. Petition for review by U. S. Circuit Court of Appeals (6) with assignments of error filed by taxpayer.
June 13. Præcipe filed—Proof of service thereon.
June 13. Proof of service of petition for review filed.

Now, June 28, 1930, the foregoing docket entries certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk, Board of Tax Appeals.

Before United States Board of Tax Appeals

Docket No. 23917

CHARLES P. LEININGER, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances: For petitioner, Irwin N. Loeser, Esq.; for respondent, John D. Kiley, Esq.

Docket entries

1927
Feb. 9. Petition received and filed. Taxpayer notified.
Feb. 11. Copy of petition served on general counsel.

1927
Apr. 12. Motion for extension to May 27, 1927, to file answer filed by general counsel.
Apr. 15. Granted. Both sides notified.
May 25. Answer filed by general counsel.
May 26. Copy of answer served on taxpayer. Assigned general calendar.

1928
Sept. 11. Motion to place on the Cleveland, Ohio, circuit calendar and to consolidate with docket 15295, filed by taxpayer. See 15295. Granted 9-28-28.

1929
Apr. 18. Notice of appearance of Irwin N. Loeser, attorney for taxpayer, filed.
May 9. Hearing set June 4, 1929, Cleveland, Ohio.
June 4. Hearing had before Ernest H. Van Fossan, on merits. Ordered consolidated with docket 15295. Stipulations read into the record. Brief due Aug. 3, 1929.
July 11. Motion for extension of time to Oct. 1, 1929, to file brief filed by general counsel. 7/12/29 granted.
July 15. Transcript of hearing of June 4, 1929, filed.
Aug. 3. Brief filed by taxpayer. See 15295.
Sept. 27. Brief filed by general counsel. See 15295.

1930
Apr. 16. Findings of fact and opinion rendered. Ernest H. Van Fossan, division 9. Judgment will be entered for the respondent.
Apr. 19. Decision entered. Ernest H. Van Fossan, division 9.
Apr. 24. Petition for reargument and rehearing filed by taxpayer. See 15295.

1929
May 8. Order denying rehearing entered.
June 10. Supersedeas bond for $18,500, approved and order filed.
June 10. Petition for review by U. S. Circuit Court of Appeals (6) with assignments of error filed by taxpayer.
June 13. Præcipe filed, proof of service thereon.
June 13. Proof of service of petition filed.

Now, June 28, 1930, the foregoing docket entries certified from the record as a true copy.

[SEAL]

B. D. GAMBLE,
Clerk, Board of Tax Appeals.

Before United States Board of Tax Appeals

Appeal of Charles P. Leninginger; address, 2231 Chatfield Drive, Cleveland, Ohio

Docket No. IT:PA:IMG:102

4 *Petition*

Filed Apr. 29, 1926

(b) Letter of April 19, 1926, from Commissioner of Internal Revenue IT:PA:I:60J:IMG:102.

(c) Amount of deficiency $3,811.75: Income tax for years 1920 and 1921; amount in controversy $3,811.75. Income tax deficiency for 1920, $1,529.15, and for 1921, $2,282.60.

(d) The Commissioner of Internal Revenue is in error—

1. In the correcting of taxpayers' income for the year 1920 from the Eagle Laundry Company by an addition of $8,230.12 to the taxpayers' reported income from same source, of $16,460.27 making a corrected total of $24,690.39.

2. In the correcting of taxpayers' income for the year 1921 from the Eagle Laundry Company by an addition of $11,342.01 to the taxpayers' reported income from same source of $11,341.92, making a corrected total of $22,683.93.

(e) The taxpayer bases his appeal from this additional assessment on the following statements of facts:

1. That the partnership owning and operating the Eagle Laundry Company while appearing on the books of record as C. P. Leininger and M. T. Monaghan, in reality consists of Charles P. Leininger and Mrs. Charles P. Leininger under a joint ownership agreement and Jane L. Monaghan, Gertrude E. Monaghan, M. A. Monaghan, Francis J. Ranney, and Donald J. Ranney by reason of sale to them by Mrs. M. T. Monaghan of her partnership interest, and that the income from the Eagle Laundry Company as distributed to C. P. Leininger and M. T. Monaghan is redistributed as follows: The share of C. P. Leininger to C. P. Leininger and Mrs. Charles P. Leininger and the share of M. T. Monaghan to Jane L. Monaghan,

Gertrude E. Monaghan, M. A. Monaghan, Francis J. Ranney, and Donald J. Ranney.

The transfer of Mrs. M. T. Monaghan's interests is evidenced by bill of sale and the evidence of joint ownership of Charles P. Leininger and Mrs. Charles P. Leininger is set forth in affidavits made a part of this petition and appeal.

On the Eagle Laundry Company tax returns for the years 1920 and 1921 the profits are allocated to C. P. Leininger and M. T. Monaghan as partners.

The history and distribution of profits as set forth in Examining Officer Cole F. Grove's report of August 27, 1925, reads as follows:

"The partnership books disclose the profits paid one-half to Mrs. M. T. Monaghan and one-half to Charles P. Leininger in 1920 and 1921.

The partnership was organized in 1904 by the above partners; however, M. A. Monaghan has always acted as agent for his mother, M. T. Monaghan.

On December 29, 1920, M. T. Monaghan sold to M. A. Monaghan, Gertrude E. Monaghan, and Jane L. Monaghan a one-quarter interest and to Francis J. Ranney and Donald J. Ranney each a one-eighth interest of her interest in the partnership. Mr. M. A. Monaghan stated the sale was made to prevent dissolution of the partnership if Mr. M. T. Monaghan should die.

Mr. Leininger did not know of the sale until advised by M. A. Monaghan several months later. Mr. Leininger immediately advised that he did not desire to become partners with all of the parties to the sale. After several conferences between Mr. M. A. Monaghan and Mr. Leininger it was verbally agreed that the partnership continue as it always had. By this Mr. Leininger desired that he deal only with M. A. Monaghan, who had always acted as agent. That no one other than Mr. M. A. Monaghan would have anything to say concerning the business.

After this verbal agreement a power of attorney was given Mr. M. A. Monaghan to act for the other parties to the sale. In 1921 under the terms of the sale, the profits, although credited on the books to M. T. Monaghan, were distributed by M. A. Monaghan as trustee, in accordance with the terms of the bill of sale to himself, the daughters and grandchildren. At the time of the sale all other assets of Mary T. Monaghan were distributed in like manner. The examiner has considered as partners all of the parties to whom M. T. Monaghan sold her interest.

Distribution of income for the year ended 12–31–1920:

C. P. Leininger ½	$24,690.39
Mary T. Monaghan ½	24,690.40

Distribution of income for the year ended 12–31–1921:

C. P. Leininger	$22,783.98
Mary T. Monaghan	22,783.94

The income creditor to Mary T. Monaghan is taxable to the following individuals whose addresses are all 10621 Detroit Ave. Cleveland, Ohio:

One-fourth	Jane L. Monaghan.
One-fourth	Gertrude E. Monaghan.
One-fourth	M. A. Monaghan.
One-eighth	Francis J. Ranney.
One-eighth	Danold J. Ranney.

Although the books of record disclose the partners as C. P. Leininger and Mrs. M. T. Monaghan, the portion of income allocated to Mrs. Monaghan is distributed and taxable to M. A. Monaghan and the daughters and grandchildren as before mentioned; in accordance with the bill of sale. In like manner the portion of income allocated to C. P. Leininger is distributed and taxable to himself and Mrs. Charles P. Leininger in accordance with a joint ownership agreement as per affidavits herein, and the income for 1920 and 1921, allocated to C. P. Leininger, was divided in accordance with the joint ownership agreement then existing and properly recorded on tax returns filed by C. P. Leininger and Mrs. Charles P. Leininger.

2. That the taxpayer in computing his income tax for the year of 1920 did report as income from the Eagle Laundry Company an amount of $16,460.27 and his partner Mrs. Charles P. Leininger did report as income for the same year and from the same source, $8,230.13 the total of these two amounts being in agreement with the amount ($24,690.40) as allocated to C. P. Leininger as his share of the profits of the Eagle Laundry Company for the year 1920.

3. That the taxpayer in computing his income tax for the year of 1921 did report as income from the Eagle Laundry Company an amount of $11,341.92 and his partner, Mrs. Charles P. Leininger did report as income for the same year and from the same source, $11,341.91 the total of these two amounts being in agreement (exception of an error of 10 cents) with the amount ($22,683.93) as allocated to C. P. Leininger as his shares of the profits of the Eagle Laundry Company for the year 1921.

(f) As stated in the foregoing each partner, Charles P. Leininger and Mrs. Charles P. Leininger, did jointly report as income the full amount received from the Eagle Laundry Company for the years in question 1920 and 1921 as allocated to Charles P. Leininger.

(g) The foregoing statements are made by me as being true and correct to the best of my knowledge and belief.

CHARLES P. LEININGER.

Subscribed and sworn to before me this 26th day of April, 1926.

AVON M. HOSE. [SEAL.]

My commission expires 9-26-28.

Now, June 28, 1930, the foregoing petition certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk, Board of Tax Appeals.

Before U. S. Board of Tax Appeals

Answer

Filed Oct. 30, 1926

The Commissioner of Internal Revenue by his attorney, A. W. Gregg, general counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer admits, denies, and alleges as follows:

(b) Admits the allegations in said paragraph of the petition.

(c) Admits the allegations in said paragraph of the petition.

(e) 1. Admits that the partners owning and operating the
8 Eagle Laundry Company in 1920 and 1921 appeared on the books and records of the said company to be C. P. Leininger and M. T. Monaghan. Denies that any other person or persons were members of said partnership, at any time during the years 1920 or 1921. Admits that in the tax returns of said Eagle Laundry Company for the years 1920 and 1921 all of the profits were allocated to said C. P. Leininger and M. T. Monaghan as partners. Neither admits nor denies that a revenue agent made a report in the words and figures set forth in said paragraph of the petition, as the making of said report is immaterial to any issue therein.

(e) 2 and 3 and (f) Admits that the taxpayer returned as income from the Eagle Laundry Company for 1920 the amount of $16,460.27, and that the wife of the taxpayer returned as income from the same source and for the same year the amount of $8,230.13, and admits that the commissioner determined that the distributive share of the taxpayer in the income of the said Eagle Laundry Company for the year 1920 was the amount of $24,690.40. Admits that the taxpayer returned as income from the Eagle Laundry Company for 1921 the amount of $11,341.92, and that the wife of the taxpayer returned as income from the same source and for the same year the amount of $11,341.91, and admits that the commissioner determined that the distributive share of the taxpayer in the income of said Eagle Laundry Company for the year 1921 was the amount of $22,683.93.

Wherefore, it is prayed that the appeal of the above-named taxpayer be denied.

A. W. GREGG,
General Counsel, Bureau of Internal Revenue,
Attorney for Commissioner of Internal Revenue.

Of counsel:
THOMAS P. DUDLEY, Jr.,
Special Attorney, Bureau of Internal Revenue.

Now, June 28, 1930, the foregoing answer certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk, Board of Tax Appeals.

9 [File endorsement omitted.]

Before United States Board of Tax Appeals

Appeal of Charles P. Leininger; address, 2231 Chatfield Drive, Cleveland, Ohio

Docket No. IT:PA:2-WSL

Petition

Filed Feb. 9, 1927

(b) Letter of December 18, 1926, from Commissioner of Internal Revenue IT:PA:2-60 D-WSL.

(c) Amount of deficiency, $5,815.99; income tax for years 1922 and 1923. Amount in controversy, $5,391.05. Income tax deficiency for 1922, $3,105.15, and 1923, $2,285.90.

(d) The Commissioner of Internal Revenue is in error—

1. In the correcting of taxpayer's income for the year 1922 from the Eagle Laundry Co. by an addition of $13, 953.28 to the taxpayer's reported income from the same source of $14,738.06, making a corrected total of $27,906.57.

2. In the correcting of taxpayer's income for the year 1923 from the Eagle Laundry Co. by an addition of $14,738.05 to the taxpayer's reported income from the same source of $14,738.06, making a corrected total of $29,476.11.

(e) The taxpayer bases his appeal from this additional assessment on the following statements of facts:

1. That the partnership owning and operating the Eagle Laundry Co., while appearing on the books of record as C. P. Leininger and M. T. Monaghan, in reality consists of Charles P. Leininger and Mrs. Charles P. Leininger under a joint ownership agreement and Jane L. Monaghan, Gertrude E. Monaghan, M. A. Monaghan, Francis J. Ranney, and Donald J. Ranney by reason of sale to them by Mrs. M. T. Monaghan of her partnership interest, and that the income from the Eagle Laundry Company as distributed to C. P. Leininger and the share of C. P. Leininger to C. P. Leininger and Mrs. Charles P. Leininger and the share of M. T. Monaghan to Jane L. Monaghan, Gertrude E. Monaghan, M. A. Monaghan, Francis J. Ranney, and Donald J. Ranney.

10 The transfer of Mrs. M. T. Monaghan's interests is evidenced by bill of sale and the evidence of joint ownership of Charles P. Leininger and Mrs. Charles P. Leininger is set forth in affidavits made a part of this petition and appeal.

On the Eagle Laundry Company tax returns for the years 1922 and 1923 the profits are allocated to C. P. Leininger and M. T. Monaghan as partners.

The history and distribution of profits as set forth in Examining Officer B. J. Monroe's report of April 29, 1926, reads as follows:

"This report does not recognize such a partnership as there is not any evidence of such, other than a division of income for income tax

purposes. Attention is invited to T. D. 3798 appearing in Bulletin V-2 as #2542 on page 15, wherein the court held that a husband, being a partner, could not form a subpartnership with his wife for the purpose of reducing the amount of partnership income taxable to him."

A perusal of the court decision referred to by the examiner "Assignment of partnership income does not avoid tax on partner" shows the case referred to therein as vastly different from this case. It is denied that there ever was an assignment of income or interest or that the partnership was formed with the purpose in view of any evasion of tax liability. The share in the Eagle Laundry Company is held jointly by C. P. Leininger and Mrs. C. P. Leininger, Mrs. C. P. Leininger's rights and claims being in the same proportion as C. P. Leininger as Mrs. C. P. Leininger worked as faithfully and diligently as C. P. Leininger in building up the business of the Eagle Laundry Company, always with the distinct understanding that each of them would have an equal interest in the enterprise.

The partnership was organized in 1904 by the above partners, however, M. A. Monaghan has always acted as agent for his mother, M. T. Monaghan.

On December 29, 1920, M. T. Monaghan sold to M. A. Monaghan, Gertrude E. Monaghan, and Jane L. Monaghan a one-quarter interest and to Francis J. Ranney and Donald J. Ranney each a one-eighth interest of her interest in the partnership. Mr. M. A. Monaghan stated the sale was made to prevent dissolution of the partnership if Mrs. M. T. Monaghan should die.

11 Mr. Leininger did not know of the sale until advised by M. A. Monaghan several months later. Mr. Leininger immediately advised that he did not desire to become partners with all of the parties in the sale. After several conferences between Mr. M. A. Monaghan and Mr. Leininger it was verbally agreed that the partnership continue as it always had. By this Mr. Leininger desired that he deal only with Mr. M. A. Monaghan, who had always acted as agent, that no one other than Mr. M. A. Monaghan would have anything to say concerning the business.

After this verbal agreement a power of attorney was given Mr. M. A. Monaghan to act for the other parties to the sale. In 1922 and 1923 under the terms of the sale, the profits, although credited on the books to M. T. Monaghan, were distributed to M. A. Monaghan as trustee, in accordance with the terms of the bill of sale to himself, the daughters and grandchildren. At the time of the sale all other assets of Mary T. Monaghan were distributed in like manner. The examiner has considered as partners all of the parties to whom M. T. Monaghan sold her interest.

Distribution of income for the year ended December 31, 1922, as shown on books:

C. P. Leininger, ½	$27,906.57
Mary T. Monaghan, ½	27,906.57

Distribution of income for the year ended December 31, 1923, as shown on books:

C. P. Leininger, ½	$29,476.11
Mary T. Monaghan, ½	29,476.11

The income credited to Mary T. Monaghan was taxable to the following individuals whose addresses are all 10621 Detroit Ave., Cleveland, Ohio, and on the following basis:

One-fourth	Jane L. Monaghan.
One-fourth	Gertrude E. Monaghan.
One-fourth	M. A. Monaghan.
One-eighth	Francis J. Ranney.
One-eighth	Donald J. Ranney.

Although the books of record disclose the partners as C. P. Leininger and Mrs. M. T. Monaghan, the portion of income allocated to Mrs. Monaghan is distributed and taxable to M. A. Monaghan and the daughters and grandchildren as before mentioned in ac-
12 cordance with the bill of sale. In like manner the portion of income allocated to C. P. Leininger is distributed and taxable to C. P. Leininger and Mrs. C. P. Leininger in accordance with a joint ownership agreement as per affidavits herein, and the income for 1922 and 1923 allocated to C. P. Leininger was divided in accordance with the joint ownership agreement then existing and properly recorded on tax returns filed by C. P. Leininger and Mrs. C. P. Leininger.

2. That the taxpayer in computing his income tax for the year 1922 did report and with certain extra assessments levied by revenue agents report an income of $13,953.29 from this source which with the corrected portion of $13,953.28 applicable to his partner Mrs. Chas. P. Leininger the total of these two amounts being in agreement with the amount of $27,906.57 as allocated to C. P. Leininger as his share of the profits of the Eagle Laundry Company for the year 1922.

3. That the taxpayer in computing his income tax for the year 1923 did report and with certain extra assessments levied by revenue agents report an income of $14,738.06 from this source, which with the corrected portion of $14,738.05 applicable to his partner Mrs. Chas. P. Leininger, the total of these two amounts being in agreement with the amount of $29,476.11 as allocated to C. P. Leininger as his share of the profits of the Eagle Laundry Co. for the year 1923.

(f) As stated in the foregoing each partner, Charles P. Leininger and Mrs. Charles P. Leininger, did jointly report an income the full amount received from the Eagle Laundry Company for the years in question 1922 and 1923 as allocated to Charles P. Leininger.

(g) The foregoing statements are made by me as being true and correct to the best of my knowledge and belief.

CHARLES P. LEININGER.

Subscribed and sworn to before me this 4 day of Feb., 1927.

[SEAL.]

D. A. BERARDI,
Notary Public.

My commission expires April 25, 1927.

18 *Affidavit of Mrs. Charles P. Leininger*

STATE OF OHIO,
Cuyahoga County, ss:

The undersigned, Mrs. Charles P. Leininger, residing at 2231 Chatfield Drive, Cleveland, Ohio, being duly sworn, says:

That she and Charles P. Leininger, her husband, are the owners of a certain share in the partnership which operates a general laundry and towel supply under the name of Eagle Laundry Company at St. Clair Avenue and East 20th Street, Cleveland, Ohio. The aforementioned certain share appears in the name of Chas. P. Leininger on the books of the Eagle Laundry Company;

That on January 1, 1920, and continuously since that time up to and including the present date, she and her husband have been owners of a share in the Eagle Laundry Company;

That the ownership of this share in the Eagle Laundry Company is and has been continuously since January 1, 1920, held and controlled by herself and her husband under a partnership agreement;

That under this partnership agreement, both the assets of the partnership, which consist chiefly of a share in the Eagle Laundry Company, and the earnings of this partnership, which consists chiefly of the partnership's share of the earnings of the Eagle Laundry Company, are to be divided equally between the undersigned, Mrs. Charles P. Leininger, and her husband, Charles P. Leininger;

That the existence of this partnership was evidenced by a partnership agreement in writing executed by the said Mrs. Charles P. Leininger, and Charles P. Leininger, her husband, on or before January 1, 1920;

That the substance of this written partnership agreement was exactly as stated above, viz, both partners to share equally in assets and earnings;

That no termination or change of or in the partnership agreement has been made since its execution, and that it is and has been in effect continuously without change of any kind since its original execution;

That this partnership agreement in writing has been lost, stolen, or destroyed without affiant's knowledge, and can not now be found;

That affiant believes it may have been burned in a fire which
14 destroyed valuable papers belonging to herself and her husband, and also may have been lost in transferring records;

That she hereby certifies as to its existence, validity and subject matter, as above outlined, during the entire years 1922 and 1923, and that it has been continuously in effect up to and at the present time.

MRS. CHAS. P. LEININGER.

Witness:

_____ _____

STATE OF CALIFORNIA,
San Diego County, ss:

Sworn to before me and subscribed in my presence this 29th day of January, 1927.

[SEAL.] E. C. BATCHELDER,
Notary Public.

My commission expires August 25, 1929.

Affidavit of Charles P. Leininger

STATE OF OHIO,
Cuyahoga County, ss:

The undersigned, Charles P. Leininger, residing at 2231 Chatfield Drive, Cleveland, Ohio, being duly sworn, says:

That he and Mrs. C. P. Leininger, his wife, are the owners of a certain share in the partnership which operates a general laundry and towel supply business, under the name of Eagle Laundry Company at St. Clair Avenue and East 20th Street, Cleveland, Ohio. The aforementioned certain share appears in the name of Chas. P. Leininger on the books of the Eagle Laundry Company;

That on January 1, 1920, and continuously since that time up to and including the present date he and his wife have been owners of a share in the Eagle Laundry Company;

That the ownership of this share in the Eagle Laundry Company is and has been continuously since January 1, 1920, held and controlled by himself and his wife under a partnership agreement;

That under this partnership agreement both the assets of the partnership, which consist chiefly of a share in the Eagle Laundry Company, and the earnings of this partnership, which consist chiefly of the partnership's share of the earnings of the Eagle Laundry Company are divded and to be divided equally between the undersigned Charles P. Leininger, and his wife, Mrs. Charles P. Leininger.

That the existence of this partnership was evidenced by a partnership agreement in writing executed by the said Charles P. Leininger, and Mrs. Charles P. Leininger, his wife, on or before January 1, 1920;

That the substance of this written partnership agreement was exactly as stated above, viz, both partners to share equally in assets and earnings;

That no termination or change of or in this partnership agreement has been made since its execution, and that it is and has been in effect continuously without change of any kind since its original execution;

That the partnership agreement in writing has been lost, stolen or destroyed without affiant's knowledge, and can not now be found;

That affiant believes it may have been burned in a fire which destroyed many of his valuable papers, and also may have been lost in transferring records;

That he hereby certifies as to its existence, validity and subject matter as above outlined, during the entire years of 1922 and 1923, and that it has been continuously in effect up to and at the present time.

CHARLES P. LEININGER.

Witness:
D. A. BERARDI.

STATE OF OHIO, *Cuyahoga County, ss:*

Sworn to before me and subscribed in my presence this 4th day of Feb., 1927.

[SEAL]

D. A. BERARDI,
Notary Public.

	R. A. R. report, 4/2/26, year 1922		R. A. R. revised, 11/8/26, year 1922		Revised assessment for appeal, 1/19/27, year 1922		1922	
Income:								
Salary	$11,203.35		$11,203.35		$11,203.35			
Partnership	27,802.41		27,906.57		13,953.29			
Dividends	1,643.00		1,643.00		1,643.00			
Total gross income		$40,648.76		$40,752.92		$26,799.64		
Deductions:								
Interest paid	124.84		124.84		124.84			
Taxes paid	237.56		237.56		237.56			
Contributions	190.00		190.00		190.00			
Total deductions		552.40		552.40		552.40		
Total net income		40,096.36		40,200.52		26,247.24		
Less exemption	2,400.00		2,400.00		2,400.00		B. R. A. additional assessment	$3,345.73
Dividends	1,643.00	4,043.00	1,643.00	4,043.00	1,643.00	4,043.00	Revised additional assessment	240.58
		36,053.36		36,157.52		22,204.24	Amount of appeal	3,105.15
Tax 4% on $4,000.00	160.00		160.00		160.00			
Tax 8% on $32,053.36	2,564.27		2,572.60		1,456.34			
Surtax on $40,096.36	2,977.34		2,996.09		1,007.20			
Total tax		5,701.61		5,728.69		2,623.54		
Previous assessment		2,382.96		2,382.96		2,382.96		
Additional assessment		3,318.65		3,345.73		240.58		

17	Year 1923		Year 1923		Year 1923		1923	
Income:								
Salary	$11,223.00		$11,223.00		$11,223.00			
Interest	50.83		50.83		50.83			
Partnership	29,823.17		29,476.11		14,738.06			
Dividends	3,146.00		3,146.00		3,146.00			
Total gross income		$44,243.00		$43,895.94		$29,157.89		
Deductions:								
Interest paid	1,115.57		1,115.57		1,115.57			
Taxes	237.77		237.77		237.77			
Contributions	480.00		480.00		480.00			
Other deductions	4,600.00		4,600.00		4,600.00			
Total deductions		6,433.34		6,433.34		6,433.34		
Total net income		37,809.66		37,462.60		22,724.55		
Capital net gain		15.50						
		37,825.16		37,462.60		22,724.55		
Less exemption	2,000.00		2,000.00		2,000.00		R. A. R. additional assessment	$2,470.26
Dividends	3,146.00	5,146.00	3,146.00	5,146.00	3,146.00	5,146.00	Revised " "	184.36
		32,679.16		32,316.60		17,578.55	Amount of appeal	2,285.90
Tax 4% on $4,000.00	160.00		160.00		160.00			
Tax 8% on $28,679.16	2,294.33		2,265.33		1,086.28		Amount of appeal, 1922	3,105.15
Tax 12½% on capital net gain	1.94		1.94		1.94		Amount of appeal, 1923	2,285.90
Surtax, $37,825.16	2,592.03		2,534.02		665.21		Total amount of appeal	5,391.05
	5,048.30		4,961.29		1,913.43			
Less 25% credit	1,262.08	3,786.22	1,240.32	3,720.97	478.36	1,435.07		
Previous assessment		1,250.71		1,250.71		1,250.71		
Additional assessment		2,535.51		2,470.26		184.36		

Now, June 28, 1930, the foregoing petition certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk Board of Tax Appeals.

18 Before U. S. Board of Tax Appeals

Answer

Filed May 25, 1927

The Commissioner of Internal Revenue, by his attorney, A. W. Gregg, General Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

(b) Admits the allegations in said paragraph of the petition.

(c) Admits that the taxes in controversy are income taxes for the years 1922 and 1923 and that the deficiencies for said years amount to to $5,815.99.

(e) 1. Admits that the partners owning and operating the Eagle Laundry Company in 1922 and 1923 appeared on the books and records of said company to be C. P. Leininger and M. T. Monaghan. Denies that any other person, or persons, were member of said partnership at any time during the years 1922 or 1923. Admits that in the income tax returns filed by said Eagle Laundry Company for the years 1922 and 1923 all of the profits were allocated to said C. P. Leininger and M. T. Monaghan, as partners in equal amounts to each.

2 and 3. Admits that the petitioner in his returns for the years 1922 and 1923 purported to return one-half of the share of the profits of said Eagle Laundry Company for each of said years allocated to the petitioner on the books of said partnership for said years.

(f) Admits that the petitioner and his wife separately returned the amount of profits from said Eagle Laundry Company allocated on its books to the petitioner for said years.

Denies generally and specifically each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the taxpayer's appeal be denied.

A. W. Gregg,
General Counsel, Bureau of Internal Revenue.

Of counsel:

Thos. P. Dudley, Jr.,
Special Attorney, Bureau of Internal Revenue.

Now, June 28, 1930, the foregoing answer certified from the record as a true copy.

[seal.]

B. D. Gamble,
Clerk Board of Tax Appeals.

Before United States Board of Tax Appeals

CHARLES P. LEININGER, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Findings of Fact and Opinion

Docket Nos. 15295, 23917. Promulgated April 16, 1930

Held that all the income earned on petitioner's share in a partnership was taxable to him, notwithstanding a contract between himself and wife that they were partners in all of his property where the books of a partnership and its income tax returns did not indicate the wife's ownership of a share, and where all profits earned were paid to the husband and deposited in a joint account.

Even if a subpartnership existed between petitioner and his wife, he would be taxable on the income received from the original partnership of which he only was a member.

Irwin N. Loeser, Esq., for the petitioner.

John D. Kiley, Esq., for the respondent.

In these proceedings redetermination is asked of proposed deficiencies for the years 1920 to 1923, inclusive, in the respective amounts of $1,529.15, $2,282.60, $3,105.15 and $2,285.90. Two issues are presented. First, the validity of the action of the board in extending time for respondent to answer, and second, the claim of petitioner that a co-equal partnership existed between him and his wife in a certain one-half interest in the Eagle Laundry Company, which one-half interest stood in petitioner's name. It was agreed by counsel that in event of a decision favorable to petitioner there would be no deficiencies for the years 1920 and 1921 and deficiencies of $240.58 for 1922 and $184.36 for 1923.

Findings of Fact

In 1898 a partnership known as Eagle Laundry Company was organized by petitioner and one M. G. Monaghan, each owning a one-half interest. In 1904 Monaghan died and his wife, Mary T. Monaghan, succeeded to his interest in the firm and on the books of the company. In 1920 Mary T. Monaghan transferred by bill of sale her interest to her children. The entire Monaghan in-
20 terest was thereafter carried on the books in the name of Marcus A. Monaghan. The partnership returns for the years 1921, 1922 and 1923 filed by Eagle Laundry Company disclose the partners to be petitioner and M. T. Monaghan and the income to be distributable one-half to each. Each of the three children of Mary T. Monaghan, however, returned a proportionate part of the income for taxation.

During the latter part of 1920 a written agreement confirmatory of a pre-existing oral agreement, was entered into between petitioner and his wife, wherein it was acknowledged that petitioner's wife had been and was a full equal partner with him in the interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses. The contract was effective from the beginning of 1920. The written agreement was not produced, probably having been lost in a fire at the plant. The fact of this transfer was communicated to Marcus A. Monaghan, who represented the owners of the other one-half interest in the Eagle Laundry Company. The Leininger interest always stood in the name of C. P. Leininger on the partnership books but Mrs. C. P. Leininger returned one-half of the profits of the Leininger interest for taxation.

Petitioner and his wife maintained prior to and throughout the period here involved a joint bank account on which each could draw unrestrictedly. The profits received from the partnership were deposited in this account by Leininger, no checks on the partnership being drawn to the wife. After the execution of the agreement the wife also maintained a small personal account in which were deposited checks received on account of earnings on her personal investments. Mrs. Leininger took no part in the management of the business and made no contribution to its capital. There was never any formal accounting between petitioner and his wife.

Petitioner never filed the contract between him and his wife with any public official or in any place of public record.

Petition was filed April 29, 1926, and a copy served on respondent May 3, 1926. On June 1, 1926, the board granted respondent's motion for 120 days' time in addition to the time allowed by the board's rules for filing an answer. The answer was filed October 30, 1926.

21 *Opinion*

Van Fossan: The first issue is resolved adversely to petitioner on authority of Shultz Bread Co., 10 B. T. A. 268.

The principal question for determination in these cases is whether petitioner is liable for tax on all of the profits of a one-half interest in a partnership or whether, under the facts, his wife may return for taxation one-half of such profits. In support of his position petitioner submits that during the latter part of 1920 a written agreement confirmatory of a pre-existing oral agreement was entered into between petitioner and his wife wherein it was agreed that petitioner's wife had been and was a full equal partner with him in the interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses.

It is observed from the testimony in the case that the books and records of the Eagle Laundry Company, the partnership, contained no entry reflecting part ownership by the wife or any payments to

her or for her account. Partnership returns for the taxable years 1921, 1922, and 1923 were sworn to by petitioner and state that the names of the partners are C. P. Leininger and M. T. Monaghan, each owning one-half. We note further than Mrs. Leininger contributed neither capital nor services to the partnership and that all checks covering profits were made to the husband and by him deposited in a joint account. This in spite of the fact that Mrs. Leininger had also a separate account in which were deposited profits on her personal investments. No accounting was every had between Leininger and his wife.

On this state of facts we are of the opinion that respondent must prevail. See George M. Cohan, 11 B. T. A. 743; affd. C. C. A. March 3, 1930; Hellman v. U. S., (Ct. Cls. May 2, 1927) A. F. T. R. 6781; Guy C. Earl v. Lucas, ——— U. S. ———, decided March 17, 1930.

Even if petitioner's wife be considered as a sub-partner or in partnership solely with her husband, the incidence of the taxing statute would not thereby be avoided, for the income earned on the one-half interest standing in the name of C. P. Leininger would first be income to him, taxable as such before its division with his wife. See Ormsby McKnight Mitchel, 1 B. T. A. 143, affd. 9 Fed. (2d) 414, 15 Fed. (2d) 287.

Reviewed by the board.

Judgment will be entered for the respondent.

Phillips dissents.

22 Now, June 28, 1930; the foregoing findings of fact and opinion certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk Board of Tax Appeals.

A true copy.
Teste:

B. D. GAMBLE,
Clerk U. S. Board of Tax Appeals.

Before U. S. Board of Tax Appeals

Decision

Pursuant to the board's findings of fact and opinion, promulgated April 16, 1930, it is

Ordered and decided, that there are deficiencies of $1,529.15 and $2,282.60 for the years 1920 and 1921, respectively.

Entered Apr. 19, 1930.

(Signed) ERNEST H. VAN FOSSAN,
Member United States Board of Tax Appeals.

Now, June 28, 1930, the foregoing decision certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk Board of Tax Appeals.

23 Before U. S. Board of Tax Appeals

Decision

Pursuant to the board's findings of fact and opinion, promulgated April 16, 1930, it is

Ordered and decided, that there are deficiencies of $3,105.15 and $2,285.90 for the years 1922 and 1923, respectively.

A true copy.

Teste:

B. D. GAMBLE,
Clerk U. S. Board of Tax Appeals.

Entered Apr. 19, 1930.

(Signed) ERNEST H. VAN FOSSAN,
Member United States Board of Tax Appeals.

Now, June 28, 1930, the foregoing decision certified from the record as a true copy.

B. D. GAMBLE,
[SEAL.] *Clerk Board of Tax Appeals.*

Before U. S. Board of Tax Appeals

Notice of filing of petition for review of decision of United States Board of Tax Appeals

To the COMMISSIONER OF INTERNAL REVENUE,
Washington, D. C.

Please take notice that a petition for review of the decisions of the United States Board of Tax Appeals in the above entitled matter, being Docket Nos. 15295 and 23917 on the Docket of the United States Board of Tax Appeals, has been this day filed with the
24 clerk of the United States Board of Tax Appeals, a copy of said petition for review being attached hereto.

(Signed) IRWIN N. LOESER,
Attorney for Charles P. Leininger, Petitioner.
800 National City Building, Cleveland, Ohio.

Service of the foregoing notice acknowledged and accepted this 2nd day of June, 1930.

(Signed) C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Before U. S. Board of Tax Appeals

Petition for review of decision by United States Board of Tax Appeals

To the Judges of the United States Circuit Court of Appeals for the Sixth Circuit:

1. Your petitioner is an individual, inhabitant and citizen of the United States and of the State of Ohio, having his residence and place of business at all times hereinafter stated in the city of Cleveland in said State of Ohio. In time and form as provided by law your petitioner filed his income-tax returns for the years 1920, 1921, 1922, and 1923 in the office of the collector of internal revenue in the said city of Cleveland, located within said sixth circuit, in which the petitioner is an inhabitant.

2. Your petitioner being aggrieved by the decisions of the United States Board of Tax Appeals made and entered on the 19th day of April, 1930, said decisions being predicated upon findings of fact and an opinion of the said United States Board of Tax Ap-
25 peals, promulgated on the 16th day of April, 1930, in the cases of Charles P. Leininger, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Dockets Nos. 15295 and 23917 on the docket of said board, prays that the said decisions of said board be reviewed by the United States Circuit Court of Appeals for the Sixth Circuit as provided by law.

The nature of the controversy before the Board of Tax Appeals was the determination of the income taxes of the petitioner for the years 1920, 1921, 1922, and 1923, the determination for the years 1920 and 1921 having been made by the said board in Docket No. 15295 and for the years 1922 and 1923 in Docket No. 23917, said cases having been consolidated for hearing, and having been heard and decided by the said board together. Your petitioner claims and has at all times claimed that the respondent and the said United States Board of Tax Appeals erroneously computed the income and the income tax liability of the petitioner for said years in the following respects, namely:

(a) As to the year 1920, by adding to the petitioner's income the sum of $8,230.12, being a portion of the net income of a partnership known as "Eagle Laundry Company," said addition to the petitioner's income being income of the petitioner's wife, said amount having been returned by the petitioner's wife as her income and being no part of the petitioner's income.

(b) As to the year 1921, by adding to the petitioner's income the sum of $11,342.01, being a portion of the net income of a partnership known as "Eagle Laundry Company," said addition to the petitioner's income being income of the petitioner's wife, said amount having been returned by the petitioner's wife as her income and being no part of the petitioner's income.

(c) As to the year 1922, by adding to the petitioner's income the sum of $13,953.28, being a portion of the net income of a partnership known as "Eagle Laundry Company," said addition to the petitioner's income being income of the petitioner's wife, said amount having been returned by the petitioner's wife as her income and being no part of the petitioner's income.

(d) As to the year 1923, by adding to the petitioner's income the sum of $14,738.05, being a portion of the net income of a partnership known as "Eagle Laundry Company," said addition to the petitioner's income being income of the petitioner's wife, said
26 amount having been returned by the petitioner's wife as her income and being no part of the petitioner's income.

By including erroneously said sums for said years as income to the petitioner, the respondent determined and the board approved deficiencies in income tax for the said years against the petitioner, in addition to income taxes for said years previously and properly computed and paid by the petitioner, in the respective amounts as follows, to wit:

For the year 1920	$1,529.15
For the year 1921	2,282.60
For the year 1922	3,105.15
For the year 1923	2,285.90

Concerning these deficiencies the respondent notified the petitioner by statutory notices of deficiency, dated respectively April 19, 1926, and December 18, 1926.

Thereupon, and within the time provided by law, to wit, respectively on the 29th day of April, 1926, and the 9th day of February, 1927, the petitioner filed his petitions at the office of the United States Board of Tax Appeals at Washington, D. C., seeking and requesting a redetermination of the said deficiencies as proposed by the respondent. The said appeals were consolidated for hearing and were heard by the United States Board of Tax Appeals on the 4th day of June, 1929. Thereafter, to wit, on the 16th day of April, 1930, the said United States Board of Tax Appeals promulgated its findings of fact and opinion, and thereafter, to wit, on the 19th day of April, 1930, made and entered its decision in which it denied the petitioner the relief sought by him in his said petitions, and affirmed the deficiencies as proposed by the respondent.

3. The errors committed by the United States Board of Tax Appeals upon which the petitioner relies, and of which he complains as a basis of this proceeding, are as follows:

(a) The board erred in including in the petitioner's income for the year 1920 the sum of $8,230.12, being income of the petitioner's wife duly returned by her as such, and arising from the partnership known as "Eagle Laundry Company."

(a) The board erred in including in the petitioner's income for the year 1921 the sum of $11,342.01, being income of the petitioner's wife duly returned by her as such, and arising from
27 the partnership known as "Eagle Laundry Company."

(c) The board erred in including in the petitioner's income for the year 1922 the sum of $13,953.28, being income of the petitioner's wife duly returned by her as such, and arising from the partnership known as "Eagle Laundry Company."

(d) The board erred in including in the petitioner's income for the year 1923 the sum of $14,738.05, being income of the petitioner's wife duly returned by her as such, and arising from the partnership known as "Eagle Laundry Company."

(e) The decision of the board is contrary to law, in that it directly conflicts with the findings of fact found by the board, and particularly to the following findings by the board, namely:

"During the latter part of 1920 a written agreement, confirmatory of a pre-existing oral agreement, was entered into between petitioner and his wife, wherein it was acknowledged that petitioner's wife had been and was a full equal partner with him in the interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses. The contract was effective from the beginning of 1920. The written agreement was not produced, probably having been lost in a fire at the plant. The fact of this transfer was communicated to Marcus A. Monaghan, who represented the owners of the other one-half interest in the Eagle Laundry Company. The Leininger interest always stood in the name of C. P. Leininger on the partnership books but Mrs. C. P. Leininger returned one-half of the profits of the Leininger interest for taxation."

Wherefore, your petitioner prays that this honorable court may review the action of the said United States Board of Tax Appeals herein complained of, reverse the decision of the said board, and direct the entry of a decision by said board in favor of the petitioner, determining that the items of alleged income to the petitioner for the said years, as set forth in paragraph 3, sections (a), (b), (c), and (d) of this petition, were improperly included by the respondent and the said board in the determination of the petitioner's income and in income tax liability for said years, and for such other
28 and further relief as may to this court appear proper in the premises.

IRWIN N. LOESER,
Attorney for the Petitioner,
800 National City Building, Cleveland, Ohio.

[*Duly sworn to by Charles P. Leininger jurat omitted in printing.*]

Now, June 28, 1930, the foregoing petition for review and proof of service certified from the record as a true copy.

[SEAL.] B. D. GAMBLE,
Clerk Board of Tax Appeals.

29 Before U. S. Board of Tax Appeals

Præcipe

To the Clerk of the United States Board of Tax Appeals:

You will please prepare a transcript of record on petition for review in the above entitled case for certification to the United States Circuit Court of Appeals for the Sixth Circuit, the said transcript to include the following, to wit:

1. The docket entries of the proceedings before the United States Board of Tax Appeals in Dockets Nos. 15295 and 23917.
2. The pleadings before the Board of Tax Appeals, including any amendments thereto.
3. The findings of fact, opinion, and decision of the said United States Board of Tax Appeals.
4. Petition for review.
5. The præcipe.

(Signed) IRWIN K. LOESER,
Attorney for Charles P. Leininger, Petitioner,
800 National City Building, Cleveland, Ohio.

Acknowledgement of service

Receipt of copy of the foregoing præcipe is hereby acknowledged this 2nd day of June, 1930.

(Signed) C. M. CHAREST,
General Counsel Bureau of Internal Revenue.

Now, June 28, 1930, the foregoing præcipe certified from the record as a true copy.

[SEAL.]

B. D. GAMBLE,
Clerk Board of Tax Appeals.

30 In United States Circuit Court of Appeals, Sixth Circuit

No. 5726

CHARLES P. LEININGER, PETITIONER

VS.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Order substituting party respondent

In the Matter of Revivor of Causes Wherein Commissioner of Internal Revenue is a Party.

It appearing to the court that there are numerous causes now pending in this court wherein Robert H. Lucas, as Commissioner of

Internal Revenue is a party—petitioner or respondent—and which causes relate to the present and future discharge of his official duties, and that on August 15, 1930, he resigned as Commissioner of Internal Revenue and that David Burnet has been appointed and has duly qualified as his successor, and is at this time Commissioner of Internal Revenue; and it satisfactorily appearing to the court that there is substantial need for continuing and maintaining each of such causes and obtaining an adjudication of the questions involved, and that this has been made to appear by motions and stipulations filed in each cause within six months from and after August 15th:

It is thereupon ordered that each said cause in which said stipulation or motion has been so filed be revived and that such cause be continued and maintained by or against David Burnet as Commissioner of Internal Revenue and as successor to Commissioner Lucas. (Sec. 780, Title 28, U. S. C.)

Entered: Nov. 14, 1930. Enter: Denison, J.

A true copy.

Attest:

[SEAL.] J. W. MENZIES, *Clerk*,
By CARL W. REUSS, *Deputy Clerk*,
U. S. Circuit Court of Appeals.

31 [Appearances of counsel omitted in printing.]

32 In United States Circuit Court of Appeals

Minute entry

(Cause argued and submitted May 12, 1931, before Denison, Hickenlooper, and Simons, JJ.)

This cause is argued by I. N. Loeser for petitioner and by M. K. Rothschild for respondent and is submitted to the court.

In United States Circuit Court of Appeals

Decree

Filed June 30, 1931

Appeal from the United States Board of Tax Appeals.

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this court that the order or decree of the said board
33 of Tax Appeals in this cause be and the same is hereby reversed, and the cause remanded for further proceedings consistent with the opinion of this court.

34 [File indorsement omitted.]

In United States Circuit Court of Appeals, Sixth Circuit

No. 5726

CHARLES P. LEININGER, PETITIONER

VS.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Petition to review an order of the Board of Tax Appeals

Decided June 30, 1931

Before DENISON and HICKENLOOPER, Circuit Judges, and SIMONS, District Judge.

Opinion filed July 2, 1931

DENISON, Circuit Judge: The taxpayer petitioner was a partner, owning a half interest in the Eagle Laundry Company, an Ohio partnership. In 1920, a written agreement was made between the taxpayer and his wife, which was confirmatory of a previous oral agreement and which declared that his wife had been and was a full equal partner with him in the interest of the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally the losses. For the years 1920 to 1923 inclusive, the commissioner included in the petitioner's taxable income the entire profits of the half interest in this company. Petitioner claims that half of these profits should have been included in the income of the wife. The commissioner ruled against the taxpayer and upon appeal the board affirmed.

We think it quite unnecessary to decide the question chiefly considered by the board—whether the wife became a partner in the laundry company, with the rights and liabilities of such a partner under the Ohio laws. In any event, she clearly owned half of the profits which, if she was not a partner, would go primarily to him.

35 If, at the moment of receiving the profits he took the legal title thereto as between the partnership and himself, she was at least at that same moment the equitable owner. She could have compelled him to pay her immediately, and he could have compelled her to pay him half of any losses. If any trouble had arisen, she could have prevented the payment of profits to him until her half interest therein was protected. It seems entirely clear to us that her share of the profits never became income received by the taxpayer.

In making the contrary holding, the board relied upon Mitchell v. Bowers, C. C. A. 2–15 Fed. (2d) 287. That case is fully distinguished from the present one, because the majority decision is rested upon the fact that the husband could cancel the arrangement at any time, and that, since the right of disposition remained his, as it does in community property, the same rule should be applied. If, how-

ever, the Mitchell case were not distinguishable, we should feel constrained to follow the reasoning of Judge Manton's dissenting opinion. The elaboration of the ruling, found in Harris v. Commissioner, 39 Fed. (2d) 546, 547, rests upon the supposed policy of the law in taxing partnerships. We do not see that section 218 (a) undertakes to fix any policy as to who is deemed to receive the income; it merely extends the definition of individual income so as to include undivided partnership profits. Lucas v. Earl, 281 U. S. 111, also relied upon, must be read in view of the comment thereon in Poe v. Seaborn, 282 U. S. 101, 117.

We can not regard this contract as a mere assignment of an interest in future profits "if, when and as" received. It creates mutual rights and liabilities; it is irrevocable; it creates, at least as between the parties, a vested interest in a property right; and the specified profits and losses were hers, not his.

In accord with our view, see Commissioner v. Barnes, C. C. A. 3–30 Fed. (2d) 289; dissenting opinions in Battleson v. Commissioner, 22 B. T. A. 455.

The order of the board is reversed, and the case remanded for recomputation in accordance herewith.

36 [Clerk's certificate to foregoing transcript omitted in printing.]

37 In the Supreme Court of the United States

Order allowing certiorari

Filed November 2, 1931

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Sixth Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Indorsement on cover:] File No. 36240. U. S. Circuit Court of Appeals, Sixth Circuit. Term No. 426. David Burnet, Commissioner of Internal Revenue, petitioner, vs. Charles P. Leininger. Petition for a writ of certiorari and exhibit thereto. Filed September 30, 1931. File No. 36240.

U. S. GOVERNMENT PRINTING OFFICE

COPY

No. 426

In the Supreme Court of the United States

October Term, 1931

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHARLES P. LAUGHLIN

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

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In the Supreme Court of the United States

OCTOBER TERM, 1931

No. ——

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

CHARLES P. LEININGER

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Sixth Circuit entered in the above cause on June 30, 1931, reversing the decision of the United States Board of Tax Appeals. (R. 30.)

OPINIONS BELOW

The opinion of the Circuit Court of Appeals (R. 31) is reported in 51 F. (2d) 7. The findings of fact and opinion of the United States Board of Tax Appeals (R. 19–21) are reported in 19 B. T. A. 621.

JURISDICTION

The decision of the Circuit Court of Appeals, reversing the Board of Tax Appeals, was rendered June 30, 1931. (R. 31.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Respondent was a member of a partnership. He agreed with his wife that she should be an equal partner with him in his interest in the partnership, but by the agreement she did not become a member of the partnership. The question presented is whether, for income-tax purposes, his distributive share of the partnership income should be reduced by the amount paid to his wife pursuant to such agreement.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1070:

> SEC. 218. (a) That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year, * * *.
>
> * * * * * *
>
> (d) The net income of the partnership shall be computed in the same manner and on the same basis as provided in section 212 * * * [with exception not material here].

The applicable section of the Revenue Act of 1921 (Sec. 218 (a) (c)), c. 136, 42 Stat. 227, 245, is identical.

Regulations 45, promulgated under the Revenue Act of 1918:

> ART. 321. *Partnerships.*—Partnerships as such are not subject to taxation under the statute, but are required to make returns of income. See section 224 of the statute and articles 411 and 412. Individuals carrying on business in partnership are, however, taxable upon their distributive shares of the net income of such partnerships, whether distributed or not, and are required to include such distributive shares in their returns. The net income of a partnership shall be computed in the same manner and on the same basis as the net income of an individual, * * * [with exception not material here].
>
> ART. 322. *Distributive shares of partners.*—The distributive share of the net income of a partnership which a partner is required to include in his return is his proportionate share of the net income of the partnership, * * *.

Articles 331 and 332 of Regulations 62 are substantially the same as Articles 321 and 322 of Regulations 45.

STATEMENT

The following facts were found by the Board of Tax Appeals (R. 19–21):

Prior to 1920 the respondent owned a one-half interest in a partnership known as the Eagle Laundry Company. (R. 19.) During the latter part of 1920, respondent entered into a written agreement with his wife, which confirmed a pre-existing oral agreement, wherein it was acknowledged that she had been and was a full, equal partner with him in his interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses. (R. 20.) The agreement was effective from the beginning of 1920. The existence of this agreement was communicated to the representative of the owners of the other one-half interest in the Eagle Laundry Company. (R. 20.) There is no finding that such representative or his principals acquiesced or refused to acquiesce in this arrangement. The respondent's entire one-half interest in the partnership continued to stand in his name on the partnership books, and the partnership returns for the years 1921, 1922, and 1923, sworn to by respondent, disclosed the partners to be the respondent and one Monaghan, and the income to be distributable one-half to each. (R. 21.) Checks representing one-half of the partnership profits were drawn payable to respondent and by him deposited in a joint bank account on which both taxpayer and his wife could draw unrestrictedly. (R. 20.) Respondent's wife took no part in the management of the business of the Eagle Laundry

Company and made no contribution to its capital. (R. 20.) There was never any formal accounting between respondent and his wife. (R. 20.)

The Board of Tax Appeals held in effect that the respondent's wife was not, by virtue of the agreement mentioned above, a partner in the Eagle Laundry Company; and that even if she were considered a subpartner or in partnership solely with respondent, the income earned on the one-half interest standing in the name of her husband would first be income distributable to him, taxable as such, before its division with her. (R. 21.)

The Circuit Court of Appeals held that under Section 218 (a) of the Revenue Act of 1918 it was unnecessary to determine whether respondent's wife became a partner since, in any event, she owned half of the profits received by her husband, so that he was only taxable on the half he was entitled to retain.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding, in effect, that it was not the purpose of Section 218 (a) of the Revenue Act of 1918 to require each individual partner to return for income-tax purposes all of his distributive share of the partnership income.

2. In holding that the agreement between respondent and his wife entitled him to deduct from his taxable income received from the partnership all payments to her under their agreement.

3. In holding that a partner may transfer his distributive share in partnership profits to one not a partner, and so escape taxation upon the partnership income received by him and paid to such transferee.

REASONS FOR GRANTING THE WRIT

1. The decision of the court below is directly in conflict with the decisions of the Circuit Court of Appeals for the Second Circuit in *Mitchel* v. *Bowers*, 15 F. (2d) 287, certiorari denied, 273 U. S. 759, and in *Harris* v. *Commissioner*, 39 F. (2d) 546, in which it was held to be the purpose of Section 218 (a) of the Revenue Act of 1918 to tax partnership income by taxing the distributive share of each partner and that a partner could not by agreement with one not a member of the partnership obtain the right to deduct from taxable income payments made or to be made to such person. See also *Hill* v. *Commissioner*, 33 F. (2d) 165 (C. C. A. 1st), certiorari denied, 281 U. S. 761.

2. The decision of the Circuit Court of Appeals is also in conflict with the principles laid down in *Bing* v. *Bowers*, 26 F. (2d) 1017 (C. C. A. 2d), affirming 22 F. (2d) 450; *Leydig* v. *Commissioner* 43 F. (2d) 494 (C. C. A. 10th); and *Rosenwald* v. *Commissioner*, 33 F. (2d) 423 (C. C. A. 7th), certiorari denied, 280 U. S. 599. In these cases it was established that so long as a taxpayer remains the owner of income-producing property, the income therefrom is taxable to him, even though

he assigns or makes a gift of such income in advance of or after receipt.

3. The decision of the court below is also in conflict with the principle laid down by this Court in *Lucas* v. *Earl*, 281 U. S. 111, where it was held (p. 115) that the tax on compensation for personal service "could not be escaped by anticipatory arrangements and contracts however skillfully devised to prevent the salary when paid from vesting even for a second in the man who earned it." The case was grounded upon the intent of Congress to measure the tax by compensation for personal service and is especially apposite here because the pertinent statute provides that in computing the net income of each partner his distributive share of the net income for the taxable year shall be included whether distributed or not. The statute plainly announces the intent of Congress to hold partners accountable for all partnership income and the decision of the court below in permitting the taxpayer to divide partnership income with one who is not a partner before the tax attaches, and so to escape a portion of the tax, is clearly contrary to the express direction of the statute and in conflict with the principle announced in *Lucas* v. *Earl*, *supra*.

4. The question is of considerable importance in administering the Federal income tax laws since it is one of frequent recurrence and is involved in cases now pending in the courts, the Board of Tax Appeals, and the Bureau of Internal Revenue.

Without a decision of this Court the Commissioner of Internal Revenue is unable to determine the proper principle to be applied in such cases, and acceptance of the decision in the present case would leave the matter in confusion because of the conflict between the decisions of different Circuit Courts of Appeals. Although the petitioner believes that in *Lucas* v. *Earl, supra,* this Court has announced the proper principle to be applied in such cases, confusion results from the fact that the Circuit Court of Appeals apparently holds that *Poe* v. *Seaborn,* 282 U. S. 101, qualifies the principle relied on in the *Earl* case. It is important in the administration of the revenue laws that all doubts with respect to the scope of the decision in the *Earl case* should be set at rest.

Furthermore, the decision of the court below would permit taxpayers who are partners to escape taxation on a part of partnership income by making similar agreements with members of their families or others not members of the partnership, and this presents a question of the gravest importance in protecting the Federal revenue against tax evasion.

Wherefore it is respectfully submitted that the petition should be granted.

THOMAS D. THACHER,
Solicitor General.

SEPTEMBER, 1931.

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No. 426

In the Supreme Court of the United States

OCTOBER TERM, 1931

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

CHARLES P. LEININGER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE PETITIONER

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In the Supreme Court of the United States

OCTOBER TERM, 1931

No. 426

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

CHARLES P. LEININGER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 17) is reported in 19 B. T. A. 621. The opinion of the Circuit Court of Appeals for the Sixth Circuit (R. 25) is reported in 51 F. (2d) 7.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 30, 1931 (R. 24). The petition for certiorari was filed September 30, 1931, and granted November 2, 1931. Jurisdiction is con-

ferred upon this Court by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether under the income-tax provisions of the Revenue Acts of 1918 and 1921, respondent may be taxed on such income, distributed to him as a member of a partnership, as he was under a duty to pay to his wife pursuant to an agreement between them by which he made her an equal partner with him in his interest in the partnership.

STATUTES AND REGULATIONS INVOLVED

These appear in Appendix A, pp. 29–31, *infra*.

STATEMENT

On petitions for redetermination of deficiencies in income taxes of respondent for the years 1920, 1921, 1922, and 1923, the Board of Tax Appeals made findings of fact (R. 16–17) of which the following is a summary:

Respondent has owned a one-half interest in the Eagle Laundry Company, a partnership, since 1898. In 1920, he and his wife confirmed, in writing, an existing oral agreement which acknowledged her as an equal partner with him in his interest in the partnership, entitled to share equally in the profits and obligated to bear equally the losses. The contract was to be effective from January 1, 1920. The fact of the transfer was communi-

cated to the representative of the owners of the other one-half interest in the Company, but it does not appear whether or not the representative or his principals acquiesced in the arrangement.

Respondent's wife took no part in the management of the business of the Company and made no contribution to its capital. It does not appear that she ever acquired or attempted to exercise any authority to act as its agent. Respondent's one-half interest continued to stand in his name on the Company's books, and its income tax returns for the years 1921, 1922, and 1923, sworn to by respondent, stated that he and M. T. Monaghan were the members of the partnership and that one-half of the income was distributable to each. (R. 16, 17, 18.)

Checks representing respondent's one-half interest in the profits of the partnership were drawn to his order. He deposited them in a joint bank account, maintained by him and his wife before and during the period in question, on which either could draw unrestrictedly. The wife also had a personal account during the period in question, in which she deposited earnings from her personal investments. Respondent and his wife never had a formal accounting. The contract between respondent and his wife was never filed with any public official or in any place of public record. (R. 17.)

The petitions and answers filed with the Board disclose the following facts:

In 1920, respondent returned for income tax purposes two-thirds of the profits he received on his one-half interest in the partnership, and his wife returned the rest. In 1921, 1922, and 1923 each returned one-half of the sums which respondent received on his one-half interest in the partnership. (R. 6, 9, 15, 17.) The Commissioner of Internal Revenue determined deficiencies for the years 1920 to 1923 on the ground that all the profits payable on respondent's one-half interest in the partnership were taxable to him. (R. 3, 6, 7.)

These determinations were approved by the Board of Tax Appeals, which held, in effect, that the wife was not a partner in the Company, and that if she were a sub-partner or in partnership with respondent alone, the income received by respondent on his one-half interest in the Company was income to him, taxable as such before its division with her. (R. 17–18.)

Respondent filed a petition for review in the Circuit Court of Appeals for the Sixth Circuit, which reversed the order of the Board (R. 24), holding that, regardless of whether the wife became a partner in the Company, half the profits received by respondent were taxable to her as equitable owner of half the sums paid him by the Company (R. 25–26).

The evidence is not reported in the record, and the findings of the Board are not challenged.

SPECIFICATION OF ERROR TO BE URGED

The Circuit Court of Appeals erred:

In holding that the agreement between respondent and his wife entitled him to deduct from the taxable income received by him from the partnership the payments due her under their agreement.

SUMMARY OF ARGUMENT

I

The Revenue Acts of 1918 and 1921 levied taxes upon the "net income of every individual" and provided that gross income should include "gains or profits and income derived from any source whatever." They also provided that individuals carrying on business in partnership should be liable for income tax only in their individual capacity and that there should "be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year."

It seems clear that if Congress had wished it could have taxed partnerships as entities. Although it treated partnership income in accordance with the doctrine of the common law, nothing in the statutes indicates that it intended to permit a further reduction of the amount of tax by partial assignments of what a partner might withdraw. We submit that no agreement or assignment in respect of the income or the partnership can relieve a partner from a tax on any of his share of the partner-

ship income unless what he has done has resulted in constituting the assignee a member of the partnership.

Practically all the decisions of the lower Federal courts are in accord with this contention.

The taxation of partnership income to the partners without regard to whether or not they are its ultimate beneficial owners is not anomolous. There are three analagous situations where one who is not the ultimate beneficial owner of income is taxed upon it—(1) where income produced by the personal services of the taxpayer is assigned, as in *Lucas* v. *Earl,* 281 U. S. 111; (2) where income earned by property or capital is assigned without assignment of the property or capital producing the income, as in a number of cases decided by several of the Circuit Courts of Appeals; and (3) where control over the source of the income is retained, although title to the producing *corpus* as well as to the income is assigned, as in *Corliss* v. *Bowers,* 281 U. S. 376.

II

Respondent's wife did not become a member of the partnership. It does not appear that the agreement purported to constitute her a member of the partnership. In order to establish that she had become a partner, it was necessary to prove that the other partners consented to such an arrangement. There is no finding that such consent existed, and all fair inferences are to the contrary. Moreover, she did not possess other powers which

ordinarily or necessarily inhere in a partner. The mere right to share in the profits of a partnership does not make one a partner. The wife's agreement to bear a share of her husband's partnership losses does not alter the situation, since her promise in that respect ran to him alone and not to the firm or the other partner.

If this Court should hold that taxability of income always follows the ownership of the income-producing *corpus*, the respondent still must fail, since the ownership of the physical and intangible assets of a partnership follows the status of a partner. Moreover, in Ohio, as elsewhere, a partner does not own a direct interest in the partnership property, but has only a right to his share of the profits, and, upon dissolution, to his share, if any, of the assets of the firm remaining after the payment of debts and adjustment of the rights of the partners *inter sese*. If a partner attempts to convey an interest in the assets of the firm, the partnership is dissolved forthwith. Here there was no such dissolution, and it does not appear that the wife asserted any claim to ownership of partnership assets. It seems clear that all the agreement was intended to accomplish was to give her the right to one-half of the profits paid respondent and possibly the right to one-half of the assets, if any, distributed to him upon the dissolution of the firm. These were merely rights against the respondent on the contract with him, and not, like his rights, against the partnership *in rem*.

ARGUMENT

I

INCOME DISTRIBUTABLE TO A MEMBER OF A PARTNERSHIP IS TAXABLE TO HIM WHETHER OR NOT HE IS THE BENEFICIAL OWNER OF THE INCOME

Sections 210 and 211 of the Revenue Acts of 1918 and 1921 (pp. 29, 30, *infra*) levy taxes upon "the net income of every individual," and Section 213 provides that gross income shall include "gains or profits and income derived from any source whatever." We submit that this language operates to impose the tax upon the entire amount of partnership income distributed to a partner even though he has agreed to pay it to another. See *Lucas* v. *Earl*, 281 U. S. 111. But any doubt left by these sections as to the intention thus to tax partnership income should be removed by Section 218 (a) of each of these Acts (pp. 29–30, *infra*), which provides:

> That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year * * *.

It seems clear that if Congress had wished, it could have treated partnerships as entities for income tax purposes, see *Burk-Waggoner Assn.* v. *Hopkins*, 269 U. S. 110, as it had for the excess profits tax. Section 201, Act of October 3, 1917, 40

Stat. 303, *infra* p. 30. Congress has, however, chosen to apply the common law rule that a partnership is to be regarded as an association of individuals rather than as an entity, and has provided for the taxation of partnership income to the partners to whom it is distributable. But, as the Circuit Court of Appeals for the Second Circuit said in *Harris* v. *Commissioner*, 39 F. (2d) 546, 547:

> Section 218 (a) did indeed continue to treat the firm income in accordance with the doctrine of the common law, in so far as it did not tax it as a whole; it allowed each partner to return only his own share, with the result that the sum of the individual taxes was less than if the firm had been taxed as an entity. It seems to us, however, that to permit a further reduction by partial assignments of so much as a partner may withdraw during the year, disregards the plan of partnership taxation, which is apparent in the section. In the first place the tax would in that case depend upon the accident of how much the partner chooses to withdraw in a given year, so offering opportunity for manipulation. In the second, the tax is imposed anyway upon the profits before distribution, and all profits must be so declared before they can be withdrawn, though in practice declaration and withdrawal may be simultaneous.

We submit that the effect of the provisions of the statute quoted above is to tax the income of a partnership to the persons who are partners at the time when the income is earned, and that no agreement [illegible] an outsider in respect of the income or

the partnership can alter or shift the obligation to pay the tax unless he becomes a member of the partnership. The agreement in the instant case did not have this result. (See pp. 23–26, *infra*.)

In the present case, respondent's wife took no part in the management of the business, and we may assume that the respondent was actively engaged in its management. Probably the formulation of the business policies of the company devolved largely upon him. If so, he determined to a considerable extent the amount of net income which his wife would receive, since the creation of gross income lay partly within his power, and still more its expenditure and thus the determination of the deductions to be made from gross income. For example, her right to receive any specific amount of net income could exist only after he had determined whether to spend the gross income in the purchase of a capital asset, or in repairs of existing property, or in payments to employees for services or bonuses, or to retain it as a reserve for the future. Apparently, under the theory advanced by the court below, the wife could not be taxed on income not distributed to her husband. Since such income is expressly taxed to the partners by Section 218 (a), respondent would be subject to the entire tax due on it. If this be the rule, then profits earned by the partnership in one year and not distributed until the next would all be taxed to the husband under Section 218 (a), but if distributed in the year when earned would be taxed one-

half to the husband and one-half to the wife under the decision of the court below.

These considerations illustrate the inconsistencies and difficulties which would be encountered in applying the test adopted by the court below, i. e., whether the agreement between the respondent and his wife was effective, *as between them,* to make her the equitable and ultimate beneficial owner of one-half of the income distributed to the respondent. We submit that no such test as this is indicated by the statute, and that the application of such a test would open the door to wholesale evasion of the scheme of partnership taxation created by Congress.

Practically all the decisions of the lower Federal tribunals are in accord with our contention.

In *Mitchel* v. *Bowers,* 15 F. (2d) 287 (C. C. A. 2nd), the plaintiff sued to recover income taxes paid on his share of the profits of a partnership of which he was a member. He asserted that he should have been taxed on only half of his share because of an agreement with his wife by which she was "entitled to one-half of the profits which shall come to" the plaintiff "from said firm" and was "liable to pay" him "one-half of the losses which he may sustain by reason of his partnership." The court assumed that the agreement did not make the wife a member of the partnership, and affirmed a judgment for the defendant Collector. This Court denied certiorari. 273 U. S. 759.

The court below in the present case (R. 25) and respondent in his brief in opposition to the petition for certiorari (p. 5) seek to distinguish the *Mitchel* case on the ground that the court there rested its decision on a provision of the contract between the husband and wife which permitted either party to terminate it at any time. The Circuit Court of Appeals for the Second Circuit has indicated in a subsequent case that the broader ground of decision stated in the quotation *supra* p. 9, was one of *two* grounds for the decision in the *Mitchel* case. See *Harris* v. *Commissioner, supra,* 39 F. (2d) 546, 547.

In *Larsen* v. *Burnet,* 50 F. (2d) 308 (Ct. App. D. C.), the taxpayer became a member of a partnership. His wife had a half interest in the funds he contributed to the partnership, and they understood that she would remain the owner of such interest. He and the wife each returned for income tax purposes half of his income from the partnership. The Commissioner took the view that all the income should have been returned by him and assessed the tax on that basis. The Board of Tax Appeals upheld the Commissioner. In the Court of Appeals the taxpayer made the same contention as was made by respondent in this case, that he became a trustee for his wife as to one-half of his investment in the partnership and also one-half of the profits accruing from the investment. In affirming the order of the Board, the Court of Appeals said (p. 309):

> We think this argument is untenable. * * * It is * * * true that appellant was accountable to his wife under the circumstances for the investment which he was managing for her. Nevertheless appellant's wife was not an actual partner in the firm, for the copartnership consisted of appellant and Forcia alone; and the applicable statute requires that the distributive share of each partner, of the net income of a partnership shall be included in the individual return of the partner for the taxable year.

In *Hill* v. *Commissioner*, 38 F. (2d) 165 (C. C. A. 1st), the members of a partnership agreed that if any of the partners died, the surviving partners would pay the estate of the deceased partner for three years following his death "sums equal to the full amount of his net profits" for each of those years. One of the partners, Soule, died. The firm was reorganized, and provision was made for the payment of the sums due Soule's estate from the profits of the new firm. The Commissioner assessed the sums paid to the estate against the surviving partners as income distributable to them. The Board of Tax Appeals and the Circuit Court of Appeals upheld the assessment. This Court denied certiorari. 281 U. S. 761.

The *Hill* case was followed in *Pope* v. *Commissioner*, 39 F. (2d) 420, 424 (C. C. A. 1st). See also *Cohan* v. *Commissioner*, 39 F. (2d) 540 (C. C. A. 2d); *Benedict* v. *Collector*, 38 F. (2d) 309, 313–314

(E. D. N. Y.). Compare *Hellman* v. *United States*, 70 Ct. Cls. 498, 512–513.

The Board of Tax Appeals has taken the same view of the statute. *Appeal of Mitchel*, 1 B. T. A. 143, 148; *Appeal of Kneeland*, 1 B. T. A. 150; *Levering* v. *Commissioner*, 5 B. T. A. 616; *Knapp* v. *Commissioner*, 5 B. T. A. 762, 766; *Hill* v. *Commissioner*, 10 B. T. A. 399; *King* v. *Commissioner*, 10 B. T. A. 698, 703; *Cohan* v. *Commissioner*, 11 B. T. A. 743, 757–758; *Harris* v. *Commissioner*, 11 B. T. A. 871, 875; *Colbert* v. *Commissioner*, 12 B. T. A. 565, 567–568; *Larsen* v. *Commissioner*, 14 B. T. A. 160; *Hill* v. *Commissioner*, 14 B. T. A. 572; *Staebler* v. *Commissioner*, 17 B. T. A. 1086; *Luce* v. *Commissioner*, 18 B. T. A. 923, 926–927; *Leininger* v. *Commissioner*, 19 B. T. A. 621 (the present case); *Heinickle* v. *Commissioner*, 20 B. T. A. 155, 160–161; *Houston Bros.* v. *Commissioner*, 22 B. T. A. 51, 63–64; *Battleson* v. *Commissioner*, 22 B. T. A. 455.

The court below cited *Commissioner* v. *Barnes' Estate*, 30 F. (2d) 289 (C. C. A. 3rd), as supporting its holding. The *Barnes* case has been cited twice by other courts. The Circuit Court of Appeals for the Second Circuit said, in *Harris* v. *Commissioner*, *supra*, 39 F. (2d) 546, 547:

> Just what were the grounds of the decision of the Third Circuit in *Commissioner of Internal Revenue* v. *Barnes*, 30 F. (2d) 289, the short opinion does not very clearly

disclose. So far as we can gather, it did not involve the point now under discussion.

The Court of Appeals of the District of Columbia said, in *Larsen* v. *Commissioner, supra,* 50 F. (2d) 308, 309:

> This decision is not touched upon by *Commissioner of Internal Revenue* v. *Barnes' Estate,* 30 F. (2d) 289, for in the latter case the wife was entitled directly to receive a share in the profits of a partnership by virtue of an assignment executed in accordance with the Uniform Partnership Act of Pennsylvania (Act of March 26, 1916), pt. 5, Sec. 27 (1), 59 P. S., Sec. 74. See *Barnes' Estate,* 7 B. T. A. 924.

See also, as to the effect of the Pennsylvania statutes, *Parshall* v. *Commissioner,* 7 B. T. A. 318. In *Heinickle* v. *Commissioner,* 20 B. T. A. 155, 161, the Board of Tax Appeals said:

> * * * in our opinion, the decision in that case [*Commissioner* v. *Barnes*] is contrary to the weight of authority.

Several decisions of the Board of Tax Appeals are relied upon by respondent. *Wing* v. *Commissioner,* 17 B. T. A. 1028, cited in his brief in opposition (p. 7), is clearly distinguishable from the present case. There the wife contributed to the capital of the partnership; took charge of the firm's bookkeeping; was a signatory of the partnership agreement, in which she was named as a partner; and was directly paid her share in the partnership

earnings. Partnerships in fact also existed in *Hinshaw* v. *Commissioner,* 16 B. T. A. 1236, and *Dickinson* v. *Commissioner,* 23 B. T. A. 1211, cited in respondent's brief in opposition at page 8. The question in the *Wing* and *Dickinson* cases was what effect should be given to the law of Michigan forbidding partnerships between husband and wife. See 23 B. T. A. 1211, 1217-1218. *Parshall* v. *Commissioner,* 7 B. T. A. 318, dealt with a Pennsylvania statute. See *supra,* p. 15. In *Kier* v. *Commissioner,* 15 B. T. A. 1114, the wives supplied the capital, and were signatories of an agreement by which, the Board found, it was the intention of all the parties to make the wives partners. Thus none of these cases are in point.

The other decisions of the Board cited in the brief in opposition are probably distinguishable on their facts. If not, they are contrary to the overwhelming weight of authority, including some of the decisions of the Board to which we have referred.

The taxation of partnership income to the partners without regard to whether or not they are its ultimate beneficial owners is not anomalous. There are three analogous situations where one who is not the ultimate beneficial owner of income is taxed upon it. Those situations are as follows: (1) Where income produced by the personal services of the taxpayer is assigned; (2) where income earned by property or capital is assigned without assignment of the property or capital producing

the income; and (3) where control over the source of the income is retained although title to the producing *corpus* as well as to the income is assigned. We shall discuss these separately.

(1) In *Lucas* v. *Earl*, 281 U. S. 111, the taxpayer and his wife agreed—

> that any property either of us now has or may hereafter acquire * * * in any way, either by earnings * * * or otherwise * * * is declared to be received * * * and owned by us as joint tenants * * *.

The question was whether the whole of the salary and attorney's fees earned by the taxpayer should be taxed to him, or only half. In holding the former, this Court said (pp. 114–115):

> A very forcible argument is presented to the effect that the statute seeks to tax only income beneficially received, and that taking the question more technically the salary and fees became the joint property of Earl and his wife on the very first instant on which they were received. We well might hesitate upon the latter proposition, because however the matter might stand between husband and wife he was the only party to the contracts by which the salary and fees were earned, and it is somewhat hard to say that the last step in the performance of those contracts could be taken by anyone but himself alone. But this case is not to be decided by attenuated subtleties. It turns on the import and reasonable construction of the tax-

> ing act. There is no doubt that the statute could tax salaries to those who earned them and provide that the tax could not be escaped by anticipatory arrangements and contracts however skilfully devised to prevent the salary when paid from vesting even for a second in the man who earned it. That seems to us the import of the statute before us * * *.[1]

Other cases falling in this group are: *Van Brunt* v. *Commissioner,* 11 B. T. A. 406; *Luce* v. *Commissioner,* 18 B. T. A. 923, 926-927; *Stack* v. *Commissioner,* 22 B. T. A. 707, 712; *Daugherty* v. *Commissioner,* No. 41905, decided by the Board of Tax Appeals on October 29, 1931, and reported in Prentice-Hall Federal Tax Service (1931), p. 2300.131; see also *Belcher* v. *Lucas,* 39 F. (2d) 74 (C. C. A. 9th). Compare *Commissioner* v. *Field,* 42 F. (2d) 820, 822 (C. C. A. 2d).

The *Earl* case and the other personal service cases cited are analogous to the present case if, as we assume, respondent was an active partner in the Eagle Laundry Company, devoting his personal services to the management of its business. The record does not reveal to what extent, if any, the payments on his half interest in the company were payments for the use of capital. The payments may have been made exclusively in return for respondent's per-

[1] The court below thought that the *Earl* case had been qualified by this Court in *Poe* v. *Seaborn,* 282 U. S. 101 (which dealt with community property), but we do not understand that the latter case had that effect.

sonal services. Respondent's wife took no part in the management of the business. (R. 17.) Therefore, even if we assume that she became the owner of one-fourth of the physical assets of the partnership by virtue of the agreement with her husband,[2] the Commissioner is entitled to prevail because of respondent's failure to establish the extent to which the income paid on his half interest in the company represented payments for the use of capital. *Larsen* v. *Commissioner*, 14 B. T. A. 160, 165. The burden rested on respondent to establish every fact necessary to his case. *Phillips, Collector* v. *Dime Trust & Safe Deposit Co.*, 284 U. S. —, No. 18 October Term, 1931, decided November 23, 1931.

(2) In *Bing* v. *Bowers*, 22 F. (2d) 450 (S. D. N. Y.), the taxpayer had assigned to his mother, by deed, an annuity "out of my share of the rents, income, and profits from my interest in all the property, real and personal" in the hands of a named company. The annuity was made a charge on his interest in the property, and the company was directed to pay the annuity to the mother. The court held that the deed did not carry an interest in the properties mentioned, but only in the net income or profits from them, and that therefore the income was taxable to the assignor. It said (p. 454):

> To permit the assignor of future income from his own property to escape taxation thereon by a gift grant in advance of the re-

[2] The Government contends that she did not become such an owner. *Infra*, p. 26–28.

> ceipt by him of such income would by indirection enlarge the limited class of deductions established by statute. As long as he remains the owner of the property, the income therefrom should be taxable to him as fully, when he grants it as a gift in advance of its receipt, as it clearly is despite a gift thereof immediately after its receipt.

The decision of the District Court was affirmed by the Circuit Court of Appeals for the Second Circuit, on the opinion of the trial judge. 26 F. (2d) 1017.

Other cases in this group are *Rosenwald* v. *Commissioner,* 33 F. (2d) 423 (C. C. A. 7th), certiorari denied, 280 U. S. 599; *Leydig* v. *Commissioner,* 15 B. T. A. 124, affirmed, 43 F. (2d) 494 (C. C. A. 10th); *Porter* v. *United States,* No. L–69, decided by the Court of Claims on November 2, 1931, and reported in Prentice-Hall Federal Tax Service (1931), p. 2300.150; *Bishop* v. *Commissioner,* No. 4517, decided by the Circuit Court of Appeals for the Seventh Circuit on December 9, 1931, reported in Prentice-Hall Federal Tax Service (1932), p. 388.

The cases in this group are analogous to the present case because, even if we assume that respondent's share of the partnership profits was paid to him wholly or partly for the use of capital,[8] nevertheless the record does not support the contention

[8] As we have indicated, *supra*, pp. 18–19, respondent has failed to show the extent, if any, to which the payments were for the use of capital.

that the agreement between respondent and his wife conferred upon her any interest in the partnership assets. See Point II, *infra*, pp. 26–28.

The following cases, where it was held that the income was taxable to the assignee and not to the assignor, may be distinguished on the ground that in them it appeared that the assignor had divested himself not only of the beneficial interest in the income but also of the ownership of the property or capital producing it: *Hall* v. *Burnet*, Nos. 5173, 5174, decided November 16, 1931, by the Court of Appeals of the District of Columbia, reported in Prentice-Hall Federal Tax Service (1931), p. 2300. 179; *Copland* v. *Commissioner*, 41 F. (2d) 501, 504 (C. C. A. 7th, distinguishing *Bing* v. *Bowers* and *Rosenwald v. Commissioner, supra*); *Commissioner* v. *Field* 42 F. (2d) 820, 822 (C. C. A. 2nd, distinguishing *Lucas* v. *Earl*, *Mitchel* v. *Bowers*, and *Harris* v. *Commissioner*, all *supra*); *Kaufman* v. *Commissioner*, 44 F. (2d) 144 (C. C. A. 3rd); *O'Malley-Keyes* v. *Collector*, 24 F. (2d) 436 (D. Conn., distinguishing *Mitchel* v. *Bowers*, *supra*); *Young* v. *Collector*, 28 F. (2d) 789 (D. N. J.); *McKee* v. *Collector*, 48 F. (2d) 838 (W. D. Okla.).

(3) In *Corliss* v. *Bowers*, 281 U. S. 376, the taxpayer had transferred property to trustees to pay the income to his wife for life with a remainder over to their children. He reserved the power to revoke or change the trust at his will. The Revenue Act provided that under such circumstances

the settlor should be taxable on the income from the trust.[4] The taxpayer's argument was that the net income from the trust had been paid to his wife; that the income never was his; that the legal title was in the trustees and the equitable title in his wife. This Court held the income from the trust taxable to the settlor, saying (p. 378):

> * * * if a man disposes of a fund in such a way that another is allowed to enjoy the income which it is in the power of the first to appropriate it does not matter whether the permission is given by assent or by failure to express dissent. The income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not.

Other cases falling in this group are: *McCauley* v. *Commissioner*, 44 F. (2d) 919 (C. C. A. 5th); see also *Mitchel* v. *Bowers*, *supra*, 15 F. (2d) 287, 289 (first ground of the decision); *Cohan* v. *Commissioner*, *supra*, 39 F. (2d) 540, 542–543; *Bishop* v. *Commissioner*, *supra*, Prentice-Hall Federal Tax Service (1932) 388, 391; *Leydig* v. *Commissioner*, See *supra*, ~~p. 10.~~ 43 F. (2d) 494–496.

The cases in this group are analogous to the present case for the reason stated by the court in *Bing* v. *Bowers*, *supra*, 22 F. (2d) 450, 454:

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[4] In *McCauley* v. *Commissioner*, 44 F. (2d) 919 (C. C. A. 5th), the court said that this provision of the Revenue Act was merely declaratory of existing law.

> * * * the power over the creation of this gross income and over the expenditure therefrom that determined the net remained in the grantor, not as a trustee of the property itself, subject to the cestui que trust's right to appeal to a court of equity, but as his personal right uncontrolled. The gross income, like the principal, the property itself, was his. The right to determine the deductions therefrom was his; only when this power had been exercised, did the net fund, or he as its owner, become charged with the duty to perfect the gift by payment to the grantee, or in any case by not preventing the grantee from receiving therefrom the amount granted to her. Not until the net was ascertained could the grantee's right attach to any specific fund. Before that the grantor had received the rents as his income from the property.

The situation in the instant case was similar. See *supra*, p. 10.

II

RESPONDENT'S WIFE DID NOT BECOME A MEMBER OF THE PARTNERSHIP

The burden rested upon respondent to prove all the facts necessary to establish the illegality of the Commissioner's determination. *Phillips, Collector* v. *Dime Trust & Safe Deposit Company*, 284 U. S. —, No. 18, October Term, 1931, decided November 23, 1931; *Burnet* v. *Houston*, 283 U. S. 223, 227;

Lucas v. *Structural Steel Company*, 281 U. S. 264, 271; *United States* v. *Mitchell*, 271 U. S. 9, 12. It was therefore essential for him to show that his wife had become a member of the partnership. Point I, *supra*. If we are in error in our belief that under the statutes only partners may return partnership income, it was at least necessary for respondent to show that his wife owned a share of the income-producing *corpus* of the partnership.

The agreement between respondent and his wife did not, we submit, make her a partner in the Eagle Laundry Company. The text of the agreement does not appear, and the findings state only that the agreement "acknowledged that petitioner's [respondent's] wife had been and was a full equal partner *with him* in the interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses." (R. 17.) (Italics ours.)

Moreover, the law and the facts indicate clearly that the wife was not a partner in the Company. In order to establish that she had become a partner, it was necessary to prove that the other partners had consented to such an arrangement. See *Pagel* v. *Creasy*, 6 Ohio App. 199, 207–208; *Cohan* v. *Commissioner*, *supra*, 39 F. (2d) 540, 542. There is no finding that such consent existed and all fair inferences are to the contrary. The partnership income-tax returns, sworn to by respondent (R. 18), stated that he and another each held a half

interest in the partnership. Compare *Bedell* v. *Commissioner*, 30 F. (2d) 622, 625 (C. C. A. 2nd). The name of respondent's wife did not appear on the books of the Company. Checks covering profits payable on the half interest standing in respondent's name were made out to him. (R. 17.) It does not appear that there ever was any accounting between her and the other members of the partnership. An Ohio statute (*infra* p. 32) requires partnerships doing business under titles not revealing the names of the partners to file certificates stating the names of the partners with the clerk of the court of common pleas. It does not appear that the name of respondent's wife was on any certificate filed by the Eagle Laundry Company. The contract between respondent and his wife was never filed in any place of public record. (R. 17.)

Furthermore, she did not possess other powers which ordinarily or necessarily inhere in a partner. She took no part in the management of the business. See *Coleman* v. *La Bounty Amusement Co.*, 21 Ohio App. 44, 49–50; *Cohan* v. *Commissioner*, *supra*, 39 F. (2d) 540, 542. She made no contribution to its capital (R. 17) and it does not appear that she contributed any services. See *Cohan* v. *Commissioner*, 11 B. T. A. 743, 757. It does not appear that she ever acquired or assumed to exercise any authority to act as agent for the Company. See *Service Co.* v. *Public Utilities Commission*, 115 Ohio St. 405, 413-

414; *Petition of Williams*, 297 Fed. 696, 702-704 (C. C. A. 1st), certiorari denied, *sub nom. Wolff* v. *Williams*, 265 U. S. 593.

The mere right to share in the profits of a partnership does not make one a partner, even where the right is directly against the partnership and not, as here, by virtue of an independent agreement with one of the partners. *Service Co.* v. *Public Utilities Commission*, 115 Ohio St. 405, *supra*; *Hayes* v. *State*, 14 Ohio Cir. Ct. (N. S.) 497, 505, affirmed, 83 Ohio St. 490; *Meehan* v. *Valentine*, 145 U. S. 611. The wife's agreement to bear a share of the losses does not alter the situation, since her promise in that respect ran to her husband alone and not to the firm or the other partner.[1]

If this Court should hold that taxability of the partnership income always follows the ownership of the income-producing *corpus*, the respondent still must fail. For here that *corpus* consisted of the physical and intangible assets of the Company. To the extent that these elements of a going business could be owned, they belonged to the partners of the Eagle Laundry Company as joint owners. As the Circuit Court of Appeals for the Second Circuit said in *Mitchel* v. *Bowers*, *supra*, 15 F. (2d) 287, 289, "ownership follows the status" of a partner.

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[1] For a discussion of the question when one becomes a partner see Douglas, Vicarious Liability, Part II, 38 Yale Law Journal 720.

Respondent argues in his brief in opposition to the petition for certiorari (p. 5) that by the agreement with him his wife became a legal or equitable owner in the assets of the company. But in Ohio, as elsewhere, a partner does not own a direct interest in the partnership property. He has only a right to his share of the profits and, upon dissolution, to his share, if any, of the assets of the firm remaining after payment of debts and adjustment of the rights of the partners *inter sese*. *Bank* v. *Carrollton R. R.*, 11 Wall. 624, 628–629; *Case* v. *Beauregard*, 99 U. S. 119, 124; *Nixon* v. *Nash*, 12 Ohio St. 647, 650; Parsons on Partnership (4th ed.), Sec. 178; Rowley, Modern Law of Partnership, Secs. 291, 292.

If a partner attempts to convey an interest in the assets of the firm, the partnership is dissolved forthwith. *Bank* v. *Carrollton R. R., supra*, 11 Wall. 624, 628; *Harris* v. *Commissioner, supra*, 39 F. (2d) 546–547. The assignee obtains only the right to the assignor's share, if any, of the assets of the firm remaining after liquidation. *Bank* v. *Carrollton, supra*, 11 Wall. 624, 629; cf. *Nixon* v. *Nash, supra*, 12 Ohio St. 647, 650. It certainly was not the intention of respondent, by the agreement with his wife, to dissolve the partnership. The business of the Laundry Company continued thereafter as it had before. The wife asserted no claim to ownership of any of the partnership assets. She did not demand dissolution and an accounting. It seems clear that all the agreement

did, or was intended to do, was to give the wife the right to one-half the profits paid respondent, and possibly the right to one-half of the assets, if any, distributed to him upon the dissolution of the firm. *Harris* v. *Commissioner, supra,* 39 F. (2d) 546, 547; *Harris* v. *Commissioner,* 11 B. T. A. 871, 874–875. These were very different rights from respondent's right as a partner. They were rights against respondent on the contract with him, and not, like his rights, against the partnership *in rem*. *Mitchel* v. *Bowers, supra,* 15 F. (2d) 287, 289; *Harris* v. *Commissioner,* 11 B. T. A. 871, 875. We submit that respondent has failed to show that his wife acquired any interest, legal or equitable, in the income-producing *corpus* of the Eagle Laundry Company.

CONCLUSION

The judgment of the court below was erroneous. It should therefore be reversed.

Respectfully submitted.

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JANUARY, 1932.

APPENDIX A

FEDERAL STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1062, 1064, 1065, 1070, 1074:

> SEC. 210. That * * * there shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax * * *.
>
> SEC. 211. (a) That * * * in addition to the normal tax imposed by section 210 of this Act, there shall be levied, collected, and paid for each taxable year upon the net income of every individual, a surtax * * *.
>
> SEC. 212. (a) That in the case of an individual the term "net income" means the gross income as defined in section 213, less the deductions allowed by section 214.
>
> SEC. 213. That for the purposes of this title * * * the term "gross income"—
>
> (a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales * * *; also from * * * gains or profits and income derived from any source whatever. * * *.
>
> SEC. 218. (a) That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share,

whether distributed or not, of the net income of the partnership for the taxable year * * *.

* * * * *

(d) The net income of the partnership shall be computed in the same manner and on the same basis as provided in section 212 * * * [exception not material here].

PARTNERSHIP RETURNS

SEC. 224. That every partnership shall make a return for each taxable year, stating specifically the items of its gross income and the deductions allowed by this title, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners.

The corresponding sections of the Revenue Act of 1921, c. 136, 42 Stat. 227, 233, 237–238, 245, contain provisions identical with those of the 1918 Act above quoted, except that Sec. 218(d), *supra*, appears in the 1921 Act as Sec. 218(c).

Revenue Act of October 3, 1917, c. 63, 40 Stat. 300, 303:

SEC. 201. That * * * there shall be levied, assessed, collected, and paid for each taxable year upon the income of every * * * partnership * * * a tax * * *.

Treasury Department Regulations 45, promulgated under the Revenue Act of 1918:

ART. 321. *Partnerships.*—Partnerships as such are not subject to taxation under the statute, but are required to make returns of income. See section 224 of the statute and

articles 411 and 412. Individuals carrying on business in partnership are, however, taxable upon their distributive shares of the net income of such partnerships, whether distributed or not, and are required to include such distributive shares in their returns. The net income of a partnership shall be computed in the same manner and on the same basis as the net income of an individual * * * [exception not material here].

ART. 322. *Distributive shares of partners.*—The distributive share of the net income of a partnership which a partner is required to include in his return is his proportionate share of the net income of the partnership * * *.

ART. 54. *Examples of constructive receipt.*— * * * The distributive share of the profits of a partner in a partnership * * * is regarded as received by him, although not distributed. See section 218 of the statute and articles 321–335. * * *

Articles 53, 331, and 332 of Treasury Regulations 62, promulgated under the Revenue Act of 1921, are substantially the same as Articles 54, 321, and 322 of Regulations 45.

APPENDIX B

OHIO STATUTES

Page's Annotated Ohio General Code, Secs. 8099, 8102, 8104:

SEC. 8099. *Certain partnerships required to file certificate.*—Except as otherwise provided in the next following section, every partnership transacting business in this state under a fictitious name, or a designation not showing the names of the persons interested as partners therein, must file with the clerk of the common pleas court of the county in which its principal office or place of business is situated, a certificate to be indexed by him, stating the names in full of all the members of the partnership and their places of residence.

SEC. 8102. *New certificate on change in membership* * * *.—On every change of the members of a partnership transacting business in this state under a fictitious name or designation which does not show the names of the persons interested as partners in the business, except in the cases mentioned in section eighty-one hundred, a new certificate must be filed with the clerk of the common pleas court as required by section eighty-hundred and ninety-nine, on the formation of such partnership. * * *

SEC. 8104. *Partnership certificate.*—Any persons doing business as partners contrary to the provisions of the next five preceding sections, shall not commence or maintain an action on or on account of any contracts made, or transactions had in their partnership name in any court of this state, until they first file the certificate therein required. * * *

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In the Supreme Court of the United States

OCTOBER TERM, 1931

No. 426

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

CHARLES P. LEININGER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONER

THE CONSTITUTIONAL QUESTION

The respondent asserts (Br. 24–26) that if Section 218 (a) be given the construction contended for by the Government, it is subject to the same infirmity as the taxing act held unconstitutional in *Hoeper* v. *Tax Commission of Wisconsin,* 284 U. S. —, decided November 30, 1931. This contention begs the question by assuming that the income which the Commissioner taxed to the respondent in the present case was the property of his wife. Whether it was her property or the respondent's

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property is one of the issues, the Government's position being that the income was property of the respondent before it was property of his wife because she was neither a partner in the Eagle Laundry Company nor an owner of its income-producing *corpus*. In the *Hoeper case* the wife "received taxable income, composed of a salary, interest and dividends, and a share of the profits of a partnership with which her husband had no connection."

RECENT CASES

The decision of the Board of Tax Appeals in *Luce* v. *Commissioner,* 18 B. T. A. 923, cited in the Government's brief on the merits at page 18, was affirmed by the Court of Appeals of the District of Columbia on January 18, 1932. The opinion is reported in Prentice-Hall Federal Tax Service (1932), at page 562. The taxpayer was a member of a law partnership. He executed an instrument by which he constituted himself trustee for his wife of one-half of the profits, salary, or other compensation or income accruing to him as a member of the firm. The wife returned these sums as her income and the husband showed them only on a fiduciary return which he filed as trustee. The Commissioner taxed these sums to the husband. The decision of the Board upholding the Commissioner was affirmed by the Court of Appeals on the authority of *Lucas* v. *Earl,* 281 U. S. 111.

Two other recent cases fall with those distinguished on page 21 of our main brief, *Ferguson, Collector,* v. *Nelson,* decided by the Circuit Court of Appeals for the Third Circuit on February 2, 1932, and reported in the United States Daily of February 5, 1932, at page 2756, and *Seatree* v. *Commissioner,* decided by the Board of Tax Appeals on January 27, 1932, syllabus in Prentice-Hall Tax Service (1932), at page 659. The former case dealt with an assignment of a contract right to royalties for the use of a patent. In the latter case, the taxpayer was a member of a partnership of accountants. The partnership agreement provided that he could retire from the firm on any June 30 by giving notice, and that in case of retirement or death, he or his representatives would receive the amount of capital he had contributed, his share of the profits to the date of retirement or death, and four shares of the profits of the partnership for the three years following the retirement or death. These payments were to be made without the rendition of any further services. He retired from the partnership on June 30, 1921. On August 3, 1922, he assigned to a trust company in trust for his daughters his right to the four undivided shares of the profits due or thereafter to become due under the partnership agreement. The trust was irrevocable. The partnership consented to the assignment, and made the payments of the four shares of the profits

to the trust company in 1922, 1923, and 1924. The Commissioner taxed these sums to Seatree. The Board of Tax Appeals upheld the ruling as to the 1922 payment on the ground that the right to that payment had accrued before the transfer in trust, but reversed the ruling of the Commissioner as to the years 1923 and 1924 on the ground that Seatree had divested himself of all ownership with respect to the payments for those years. The Board said that it was conceded that Seatree was one of the partners largely responsible for the growth and good will of the firm and that the payments for three years were compensation for his interest in the good will, which was in the nature of a capital asset; and it held that the assignment was of a property right, and not merely of income to accrue in the future.

CASES ON THE PARTNERSHIP QUESTION

On pages 8 and 12 of the respondent's brief cases are cited which are said to support the respondent's contention that by the agreement with his wife she became either a partner in the Eagle Laundry Company or the equitable owner of half of the respondent's interest in the Company. Since we believe that the partial quotations from these cases appearing on pages 8, 12, and 13 of the respondent's brief give an inaccurate picture of the applicable law, we have abstracted, and quoted fully from, the cases cited by the respondent.

Rosenstiel v. *Gray*, 112 Ill. 282, was a bill by Gray, Sunderland, and Robey for the settlement of partnership accounts against Rosenstiel. Originally, Gray, Sunderland, and Rosenstiel were members of a copartnership which manufactured and sold woolen goods under the name of C. H. Rosenstiel & Co. In March, 1873, Gray and Sunderland sold an undivided one-third of their interest in the business to Robey. The business continued until June, 1873, when Rosenstiel sold all his interest in the firm to others. "The bill prayed an accounting of all the co-partnership business from the time of its commencement up to the time of the termination of the same by the sale by Rosenstiel * * *." As to Rosenstiel's sale, the court said (p. 288):

> What Rosenstiel sold to Thompson and Blanchard was his one-third interest in the partnership property. This interest was something, only, which would be remaining after the payment of this firm's liability for * * * advances and other partnership debts, the rule being, that *the purchaser of an interest of one of the co-partners in partnership property acquires only such interest as the vendor had, and that is, his share of the residue after the affairs of the partnership are wound up and the debts paid* * * *. (Italics ours.)

The court also said (pp. 291–292):

> It is urged that there was error in finding and decreeing payment to Robey, because

Rosenstiel never consented that the latter should become a member of the firm. It appears that Robey acquired an interest in the firm in March, 1873, by purchase from Sunderland and Gray, and that *the firm name was then changed* to Gray, Robey & Co. All this, it is said, was done without the knowledge or consent of Rosenstiel. Although there be no direct evidence of any actual knowledge of or consent to the admission of Robey to the firm on the part of Rosenstiel, yet, from the length of time which elapsed from Robey's purchase into the firm, and change of the firm name, until the sale of Rosenstiel's interest in June, 1873, with no objection appearing on the part of Rosenstiel, there would be ground of inference of an implied acquiescence by Rosenstiel in Robey's becoming a member of the firm. But supposing Robey was not a partner with the consent of Rosenstiel, he was a joint owner with Gray, Sunderland and Rosenstiel at the time Rosenstiel went out of the firm, and as such was a necessary party to any suit for a distribution of the assets, and might, we think, not improperly, have a decree for any sum that might be found due him on account of the firm property, and even against Rosenstiel. It caused no increase of the amount found due from Rosenstiel, and *we do not perceive that it made with him any essential difference, or afforded any substantial cause of complaint, that he was decreed to pay a portion of such amount to Robey, who was entitled thereto,*

instead of the whole amount to the two other partners. (Italics ours.)

The *Rosenstiel case* differs from the present case in three important respects. 1. It was the intent of the parties involved in the transfer to Robey that he should become a partner. In the present case it does not appear that respondent and his wife intended by their agreement to make her a partner in the Laundry Company, nor does it appear from the statement of the agreement in the findings of fact that the agreement purported to constitute her such a partner. 2. The firm name was changed to include that of Robey. There was no change in the firm name in the present case. 3. The effect of holding that Robey became either a partner or a joint owner of the firm assets was merely to uphold the decree in favor of Robey as against Rosenstiel. In any case, Robey would have been entitled to the same share as against Gray and Sunderland. As the court was careful to point out, it made no difference to Rosenstiel whether he paid Robey directly, or indirectly through the other partners. In the present case decision of the question affects substantial rights of the parties.

In *Smith-Powers Logging Co.* v. *Bernitt,* 237 Fed. 570 (C. C. A. 9th), Bernitt and others entered into an agreement with a firm known as Dean & Co., which owned tide lands, to construct and operate log booms upon the lands. The parties to the agreement were to share in the proceeds and con-

tribute to the maintenance of the booms in stated proportions. The property of Dean & Co. eventually came into the hands of the Smith-Powers Logging Co., and the interest of Bernitt and the others into the hands of the plaintiffs in this suit, who sought to recover their interest in the booms and their share of the proceeds of its operation. The trial "court found from the record that all the successors in interest to Dean & Co. recognized the agreement and treated with Bernitt and his associates and successors strictly according to the terms thereof, and that the appellants can not now controvert the appellees' interest in the booms." In affirming a decree for the plaintiffs, the Circuit Court of Appeals said (p. 572):

> The appellants contend that the testimony fails to show any partnership between the copartnership of E. B. Dean & Co. and the predecessors in interest of the appellees. The evidence, however, shows clearly that the original agreement was that of a *joint venture*. The final situation was complicated by the changes that subsequently occurred, such as the retirement of Young and Klahn. But through all the changes the business continued to be operated as before, without any objection upon the part of Dean & Co. or any one. From the conduct of the parties, the court below was clearly justified in holding that there was consent to the changes in membership by the concurrence of all the parties, evidenced by their conduct.

> It is well settled that, with such concurrence, the purchaser of an interest may become a partner with the consent of all the parties, either expressed or implied from their conduct. [Citations.] *But it is not important to inquire how long the partnership continued to exist.* The important fact is that the predecessors in interest of the appellees were induced by E. B. Dean & Co. to enter upon lands which the latter owned and to contribute one-half the expense of constructing booms thereon, with the understanding that all parties were to have a joint interest in them, and that the booms were operated under that understanding until the appellees were ousted. (Italics ours.)

Thus in this case also the result would have been the same whether or not there was a partnership, and it is not clear that the court's decision rested on a finding of continued partnership. Moreover, the Circuit Court of Appeals had before it a finding by the lower court on the evidence that all the parties had consented to the changes in "membership." In the present case there is no such finding.

In *Nirdlinger* v. *Bernheimer,* 133 N. Y. 45, the plaintiffs were the representatives of Frederick Nirdlinger, who had been a subpartner with his brother Jacob in a joint venture. The suit was for an accounting against the representatives of Jacob and against Bernheimer, one of the joint adventurers. Frederick had had a half interest in the funds which Jacob contributed to the joint venture, and

the brothers had agreed that Frederick was entitled jointly with Jacob in the latter's share of the property acquired by the joint adventurers, and should share equally in the burdens imposed on Jacob by the joint venture. The agreement was not made known to the other joint adventurers. The trial court entered an interlocutory judgment in favor of the plaintiffs, which the intermediate appellate court reversed upon the appeal of Bernheimer, the representatives of Jacob having acquiesced in the judgment. In the Court of Appeals, Bernheimer argued that Frederick had forfeited his interest by his failure to bear his share of the burdens of the joint venture imposed upon Jacob. In reversing the order of the intermediate appellate court and affirming the judgment of the trial court, the Court of Appeals of New York said (pp. 53, 54, 55):

> We are unable to see how the defendant Bernheimer can avail himself, upon this appeal, of any such question. Jacob Nirdlinger's representatives have acquiesced in the judgment, and as Frederick was only a subpartner of Jacob's, not known to the other members of the firm, and having no other or greater rights in the firm property than those which he acquired by assignment from his brother, it is not seen how any of the partners, other than Jacob, or his representatives, can take advantage of any failure on Frederick's part to comply with the conditions upon which he acquired an interest in his brother's share of the co-

partnership estate. He owed no duty to the common enterprise. His obligation was to his brother. If the later is not in default in defraying his share of the burden of the joint-adventure, the failure of the former to reimburse him is available to him alone as a defense. The defendant Bernheimer is not prejudiced; he can only be required to account for Jacob's share of the property, and *it is immaterial to him whether the whole share is paid to Jacob or divided between him and Frederick's representatives.*

The right of a sub-partner to maintain an equitable action of this character upon the facts disclosed in this case can not be successfully questioned. As between themselves the brothers were partners, and the subject of the partnership is the interest which one of them had in the Minnesota enterprise, and the extent of which must be determined in order to adjust the equities between them. By the death of the brother's intestate their respective rights have, by operation of law, become vested in their heirs and legal representatives, and if for no other reason the settlement and distribution of their estates would render an accounting necessary. The property in which both estates have a joint interest is in the hands of Bernheimer as trustee, and his presence as a party defendant is authorized both under sections 447 and 452 of the Code; the former of which provides that a person may be made a defendant who is a necessary party for a com-

plete determination or settlement of a question involved therein; and the latter imposes upon the court the duty of directing persons to be brought in whose presence is required for a final disposition of the controversy. [Citations.]

The case of *Burnett* v. *Snyder* (81 N. Y. 550) is relied upon by the respondent; but is not applicable. The subpartner there made no contribution to the capital of the principal firm, and had no proprietory interest in its funds, or in the profits arising in its business before their division, and the question involved related solely to his liability to the creditors of the firm. Here the plaintiffs have a vested interest in the corpus of the enterprise, and the relation of subpartners has been terminated by the death of the parties to it, and the time has arrived when equity requires that the status of all the parties having a right to share in the partnership investments shall be ascertained.

* * * * *

The admission of plaintiffs' right to maintain this action as the successors and representatives of a subpartner of one of the members of the defendant's firm, is not antagonistic to the principle of personal selection, or *delectus personarum*, as it is sometimes called, which is usually the controlling motive in the formation and pursuit of partnership adventures. *The defendants are not compelled to admit the plaintiffs as members of their firm. It is still Jacob*

> *Nirdlinger's interest in the enterprise which is to be the subject of adjudication,* and the plaintiffs are concluded by his dealings with the firm, and by his acts and attitude with reference to its affairs. Payments made to him are chargeable to them; his defaults, if any, are imputable to them, and if the defendant Bernheimer has annually rendered accounts to him, which, as between them, have become accounts stated, they will be given a like effect upon the accounting which has been ordered in this action, and can not be avoided, except upon some ground which would ordinarily be sufficient to open such an account, as for fraud, collusion, mistake or the like.
>
> In short, the defendants are to be placed in no other or worse position than if this action had been brought and prosecuted by Jacob Nirdlinger, for the purpose of an accounting and a discovery of his interest in the common property. (Italics ours.)

The questions in *Nixon* v. *Nash,* 12 Ohio St. 647, were whether a judgment creditor of a partner could, after execution returned unsatisfied, levy upon the partner's interest in the firm, and if so, the effect of such levy. The plaintiff had made such a levy and the suit was for an accounting of the interest of the judgment debtor in the assets of the firm. A demurrer was sustained by the trial court and the intermediate appellate court affirmed. In reversing and remanding for further proceedings, with directions to overrule the demurrer, the

Supreme Court of Ohio said that the interest of a partner could be subjected to the payment of a judgment against him, but that the authorities differed widely as to the course to be pursued by the creditor and the officer executing the writ. It continued (pp. 649–650):

> * * * the decided weight of authority seems to be, that the officer may, and, for his own security and that of the execution creditor, should take possession of all the chattels levied on, and after the sale of the debtor's interest therein, redeliver the same to the other partners *and* the purchaser, who are said to be tenants in common of the chattels so sold.
>
> The levy and sale must be of an undivided interest in the chattel, corresponding to the debtor's share or nominal interest in the firm; but it is also well settled, that the separate creditor or the purchaser at such sale acquires only the beneficial interest of the debtor partner in the articles sold. *Each partner holds his interest in the joint property, subject to a trust for the partnership creditors, and the claims of his several copartners; so that the beneficial interest of each, is his residuary share after the partnership accounts are settled, and their rights, inter sese, adjusted.*
>
> *The seizure and sale is, pro tanto, at least, a dissolution of the partnership, and calls for an adjustment of the joint business.* If the partnership is then entirely solvent, the beneficial interest of the debtor in the arti-

> cles sold, may equal his proportionate share in the joint business; but if not so, a part, if not the whole, of his interest therein, may be required to liquidate the balance due from him on the final adjustment. (Italics ours.)

The court concluded that convenience demands that the levying creditor be permitted to ascertain the extent of his debtor's interest in the partnership assets by a suit for an accounting against the other partners.

Parish v. *Bainum*, 306 Ill. 618, was a suit by Parish for an accounting of the affairs of a partnership, which it was alleged was created by a contract signed by the parties. Excerpts from the opinion follow (pp. 622, 624):

> It is insisted that there was no partnership. The contract clearly provided for a trading venture in land, in which Parish was to furnish the purchase price, Noah C. Bainum was to purchase the property in his own name, manage and dispose of it, the other two parties with him were to guarantee Parish against loss, so far as two-thirds of the purchase price was concerned, by giving their note for two-thirds of the purchase price advanced by him, and all the parties to the agreement were to share in the profits in the proportions fixed by the contract. The parties engaged in such an enterprise, though no general partnership exists, are partners in the particular transaction. [Citations.]
>
> * * * * *

> when Parish failed to advance the $15,000 and it became necessary for the other partners to raise the rest of the purchase price, Noah C. Bainum went to Hall, the president of the First National Bank of Carmi, to procure the money, and arranged with him to advance $1,000 personally and take one-twentieth interest in the partnership. This was a personal arrangement between Noah C. Bainum and Hall. There is no evidence that the other partners consented to it or accepted Hall as a partner. *The purchaser from one partner of his interest in the partnership without the consent of his partners that the purchaser shall become a partner does not become a partner by reason of his purchase but merely the owner of the proportion which his vendor held in the partnership after the closing up of the partnership and the payment of the partnership debts.* (Italics ours.)

Sherk v. *First National Bank,* 152 S. W. 832, was an action by Sherk, a member of the partnership of Sherk & Stenek, against the holders of partnership property by deed of trust from Stenek. The trial court directed a verdict for the defendants. The Texas Court of Civil Appeals, after detailing the facts, said (p. 834):

> The appellant, by various assignments, complains of the action of the court in instructing a verdict for appellees, on the ground that when the deed of trust was executed by Stenek to appellees the partnership

of Sherk & Stenek was insolvent; that said firm owed appellant large sums of money, and he was entitled to a partner's lien on said lots before outside debts were paid; and that, if appellees were entitled to recover anything, it was no more than the interest of James Stenek in the property after all the firm debts of Sherk & Stenek were paid, and, as the debts were in excess of the property, the appellant [*sic*] took nothing by its deed of trust.

* * * * *

It may be said generally *the right of the partner is in effect a right to share in the surplus left after discharging all the firm debts,* including the reimbursement to the partner for advancements made by him in excess of his proportional share. Each partner has the right to require all the firm assets to be applied to the payment of the firm debts. But this right of a partner is property and can be sold and transferred. It is effectually sold and transferred by the sale and transfer of all the interest in the firm property whether to his partner or to a stranger. *Such a sale and transfer dissolves the partnership* and extinguishes the right the partners have in the property as partnership assets. (Italics ours.)

The judgment was affirmed on the ground that after the execution of the deed of trust by Stenek and its recordation, Sherk purchased from Stenek the latter's entire interest in the partnership, Sherk

assuming the debts of the firm and waiving his lien on the property of the partnership which Stenek had conveyed to the defendants.

Stokes v. *Stevens,* 40 Cal. 391, was an action of replevin to recover grain in the possession of the defendants under writs of attachment. The grain had been owned by Neuart and Young as partners, but Neuart had sold it to the plaintiffs in satisfaction of his personal indebtedness to them. The grain was in a warehouse, and the defendants sued out the writs of attachment on the grain to recover an indebtedness to them by the partnership of Neuart & Young. The trial court gave judgment for the plaintiffs. The defendants contended that Neuart had no power to convey the partnership property in payment of his individual debts as against the creditors of the firm. The Supreme Court of California said (pp. 394–395):

> The legal title to partnership property is in the copartners, either of whom has authority to convey it in any transaction within the scope of the partnership. It is equally plain that each copartner has an unlimited power of disposition of his share of the partnership property, subject only to the claims of creditors of the firm, and of the other copartners on a settlement of the partnership affairs. If the firm owes no debts, and if there be nothing due from one of the copartners to the others, he clearly has the right, at his option, to sell and convey his interest in the partnership property, un-

less he be restrained from so doing by the terms of the copartnership. But the claims of the creditors of the firm, and of the other copartners, are only in the nature of an equitable lien on the partnership property, for the security, in the one case, of the demands of the creditors, and in the other, of the remaining copartners, for any balance found to be due to them on a settlement of the partnership affairs. This lien can only be asserted in a Court of equity, which has the adequate machinery for winding up the partnership, marshaling the assets and ascertaining the debts due from the firm, and the balances, if any, due to the several copartners. * * * So long as the legal title of the partnership property remains in the copartners, a creditor of the firm may pursue his remedy against it, in an action at law, in the same manner as against an individual debtor. But if the legal title has been conveyed to a third person *bona fide*, the creditor can pursue the property only by a bill in equity to marshal the assets and enforce his equitable lien. The defendants in this case did not pursue this remedy, but, treating the sale to the plaintiffs as absolutely void, have seized the property under an attachment at law. It may be said, however, that, even though it be conceded that Neuart had the power to convey to the plaintiffs the legal title to his own interest in the grain in payment of his own individual debt, he had no power to convey the legal title to Young's interest for such a purpose; and,

consequently, that Young's interest remained unaffected by the sale to the plaintiffs, and was, therefore, subject to the attachment.

But if it be admitted that the legal title to Neuart's interest only passed to the plaintiffs, the result of the transaction was to constitute the plaintiff's tenants in common with Young of the legal title, subject to the claim of the creditors of the firm, which, as we have seen, could only be asserted, as against the plaintiffs, in a Court of equity; and the plaintiffs, being in possession, had the right to retain it as against their co-tenant, Young, or any one claiming under him. If Young's interest was subject to seizure under attachment, the levy should have been upon that interest only, and not upon the whole of the grain, thereby ignoring the plaintiffs' title to any part of it. But it may be, that Young consented to the sale by Neuart to the plaintiffs, and if so, they acquired thereby the legal title to the whole. It is clear, that if Young consented to, or authorized the sale of the grain, by Neuart to the plaintiffs, they acquired the legal title of the whole; and we must presume, in support of the judgment, that the Court found it as a fact, that Young did so consent to and authorize the sale. For these reasons, I think the defendants have mistaken their remedy, and that the judgment ought to be affirmed.

Van Brocklen v. *Smeallie*, 140 N. Y. 70, was an action for damages for breach of a contract to pur-

chase the interest of the plaintiff in a copartnership. The sole question in the case was the measure of damages applicable to such a breach. The trial court gave judgment for nominal damages, and the intermediate appellate court affirmed. In reversing the judgment, the Court of Appeals of New York said (p. 74):

> The rule of damages applied was that which pertains to sales of real property, and which differs in scope and in principle from that applicable to sales of personalty. The opinion describes the contract as one for "the purchase of land," and all the authorities cited relate to sales of real estate. They have no application to the case in hand. The plaintiff had no land to sell and did not contract to sell any. What he did bargain about was his ultimate interest in the partnership assets when converted into money and after payment of all debts. His share of the net surplus then remaining was the only subject of sale, and all that he contracted to sell. His vendee would not and could not become a partner by force of the purchase, would gain no title to the assets as such and could only force a sale of such assets, including the mill, and the distribution of the proceeds. It was said in *Tarbell* v. *West* (86 N. Y. 287), that "it is now well settled that *a purchaser from one partner of his interest in the partnership, acquires no title to any share of the partnership effects, but only his share of the surplus, after an*

accounting, and the adjustment of the partnership affairs." The courts below, therefore, proceeded on a wrong basis, which led them into error. (Italics ours.)

Keith & Son v. *Ham,* 89 Ala. 590, was an action by J. N. Ham and P. J. Ham against Keith & Son to recover damages for the conversion of cotton on which the plaintiffs claimed to hold a mortgage. The complaint alleged that one Martin gave a mortgage on the cotton to the firm of Ham & Collins (composed of J. N. Ham and Collins) and that Collins transferred his interest in the mortgage to P. J. Ham. On appeal from a judgment for the plaintiffs, the Supreme Court of Alabama said, in affirming the judgment (p. 593):

> It is immaterial what effect the assignment by Collins of his interest in the property belonging to the firm of Collins & Ham had upon the partnership, or whether the assignee and Ham constituted a new partnership. The assignment, at least, operated to vest Collins' interest in the assignee, and to make him, jointly with the other partner, the owner of the assets which had belonged to the partnership, among which was the mortgage covering the cotton alleged to have been converted. And *this suit was instituted, and properly so, by these joint owners, or owners in common, as such, and not upon any theory of a new and continuing partnership.* It was shown that the mortgage, and a note for the amount secured by it, were executed to Collins & Ham. The transfer by Collins

> to P. J. Ham was sufficiently specific to invest the latter with the former's interest. It further appeared that both the note and mortgage came to the possesion of P. J. and J. N. Ham. The objections taken in the court below, on the ground of a want of interest in P. J. Ham, were, therefore, properly overruled. (Italics ours.)

We submit that none of these cases support respondent's contention that by the agreement with his wife she became either a partner in the Eagle Laundry Company or a joint owner of its income-producing *corpus*. Many of the cases were suits for accounting of defunct partnerships. The problem before the courts in such cases is substantially different from that raised by the present case. To give the subpartner a direct right of action against the other partner is merely to eliminate one procedural step in the interest of convenience. In such elimination there is no violation of the fundamental principle of partnership law that the consent of the partners is required to make an outsider a member of the partnership.

We submit that the extracts quoted from the text books on pages 11–12 of respondent's brief do not give the views of the authors completely, and that a reading of all of the sections from which extracts are quoted will disclose that they are not at variance with our contentions.

We also wish to call the Court's attention to a misquotation of the Government's argument by

the respondent. On page 27 of the respondent's brief, the respondent quotes the Government's brief as follows:

> We submit that no agreement or assignment in respect of the income *of* the partnership can relieve a partner from a tax on all of his share of the partnership income * * *

Our argument, as stated on page 5 of our brief, is:

> We submit that no agreement or assignment in respect of the income *or* the partnership can relieve a partner from a tax on any of his share of the partnership income * * *

Respectfully submitted.

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CHARLES ELMORE

In the Supreme Court of the United States

OCTOBER TERM, 1931.

No. 426.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

CHARLES P. LEININGER,
Respondent.

BRIEF OF RESPONDENT
In Opposition to Petition for Writ of Certiorari.

LEVI COOKE,
GEORGE R. BENEMAN,
Union Trust Bldg., Washington, D. C.,
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THE GATES LEGAL PUBLISHING CO., CLEVELAND, O.

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In the Supreme Court of the United States

OCTOBER TERM, 1931.

No. 426.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.,

CHARLES P. LEININGER,
Respondent.

BRIEF OF RESPONDENT
In Opposition to Petition for Writ of Certiorari.

The "Opinions Below" and Jurisdictional facts are as stated by the petitioner.

STATEMENT OF CASE.

The United States Board of Tax Appeals (hereinafter referred to as The Board) made "Findings of Fact" (R. 19-20) from which it appears

(1) Prior to 1920 respondent owned a one-half interest in a partnership known as the Eagle Laundry Company. (R. 19.)

(2) In 1920 respondent entered into a written agreement with his wife, confirmatory of a pre-existing oral agreement, "wherein it was acknowledged that" his "wife had been and was a full equal partner with him *in the interest* in the Eagle Laundry Company." (R. 20.)

(3) "The fact of this transfer (R. 20) was communicated" to the owners of the other half interest in the Laundry Company.

This proceeding, as presented to the Circuit Court of Appeals, involved the single question, the Board having found specifically the foregoing facts, and particularly that respondent's "wife had been and was a full equal partner with him *in*" *his "interest"* in the partnership, was the income attributable to the wife's share her taxable income or that of the respondent? The position of the respondent, sustained by the Circuit Court of Appeals, is that, prior to the agreement of 1920 as found by the Board, the respondent had a vested interest as a partner in the laundry company: that, prior to the accrual of the income here involved he transferred to his wife, according to the findings, a half interest in his vested interest as a partner: and hence, when profits accrued, they were attributable one-half to the respondent's interest and one-half to the interest of his wife—when a check or other medium, evidencing a distribution of partnership profits, was issued and delivered to him and deposited by him in their joint account (R. 20) he was *eo instanti* he received the fund the holder thereof as to one-half in his own right and as to the other half as trustee for his wife: and the latter moiety was his wife's and not his taxable income.

ARGUMENT.

One serious fallacy runs through the petitioner's brief and vitiates its entire argument. It assumes (p. 6) that the 1920 agreement as found by the Board amounted only to a transfer by respondent to his wife of a share of profits—an assignment or gift of income. The agreement in question was far more fundamental. According to the findings it constituted the respondent's wife "a full equal partner with him" in his interest in the laundry company. Hence the court below said in its opinion:

> "We cannot regard this contract as a mere assignment of an interest in future profits 'if, when and as' received. It creates mutual rights and liabilities; it is irrevocable; it creates, at least as between the parties, a vested interest in a property right; and the specified profits and losses were hers, not his."

The rule of law, applicable to the facts, recognized by this Court as well as by the various Circuit Courts of Appeals and the Board, was well stated by the Board in *Leydig v. Commissioner,* 15 B. T. A. 124, 132, affirmed 43 Fed. (2d) 494 (C. C. A. 10th):—

> "The cases * * * are singularly free from conflict as to the principle governing the issue raised. From them we conceive the rule to be that income *per se* cannot be assigned to relieve the assignor of the tax levy, but, where the thing assigned was a property right, real or personal, productive of income, income thereafter arising from such property is income to the assignee by virtue of his ownership."

The petitioner assigns "four reasons for granting the writ" of certiorari which we shall examine briefly.

1. While section 218(a) of the Revenue Acts of 1918 and 1921 did provide that "there shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership," the court below was right on authority when it said of this provision (R. 32):

> "We do not see that section 218(a) undertakes to fix any policy as to who is to be deemed to receive the income; it merely extends the definition of individual income so as to include undivided partnership profits."

The Sixteenth Amendment to the Constitution was not intended to authorize the taxation of one person on

another's income. Neither does the statute or any section thereof require that such be done. Section 218(a) relied upon by the petitioner did not impose any tax. Section 210 imposed the tax on individuals in the following words:

> "Section 210 * * * there shall be levied * * * upon the net income *of* every individual a * * * tax at the following rates."

The sole purpose of Section 218(a) was to provide that partnerships as such should pay no tax, but rather that the tax due on the profits earned by a partnership whether distributed or not should be paid by the owners of the business in their individual capacities. To tax the respondent upon income in which he had no beneficial interest would run counter to the definition of taxable income laid down by this Court in *Eisner v. Macomber,* 252 U. S. 189, 207 as being "gain * * * derived, that is received or drawn by the recipient *for his separate use, benefit and disposal.*" In *Poe v. Seaborn,* 282 U. S. 101, this Court said:

> "These sections lay a tax upon the net income of every individual. The act goes no farther, and furnishes no other standard or definition of what constitutes an individual's income. The use of the word 'of' denotes ownership. It would be a strained construction, which, in the absence of further definition by Congress, should impute a broader significance to the phrase."

To tax to an individual income not beneficially owned by him would obviously cast grave doubt upon the constitutionality of the statute. As said by the Circuit Court of Appeals (8th) in *Central Life v. Commissioner,** .. Fed. (2d):

> "* * * a cardinal purpose of the income tax laws is to tax the income to the person who has the right or beneficial interest therein, and not to throw the burden

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*Not yet officially reported: decided July 13th, 1931.

upon a mere collector or conduit through whom or which the income passes."

(*Shellabarger v. Commissioner*, 38 Fed. (2d) 566, 567, C. C. A. 7; *Bettendorf v. Commissioner*, 49 Fed. (2d) 173 C. C. A. 8.)

The cases cited by petitioner neither support his claims nor are they in conflict with the decision of the court below in the instant case. *Mitchel v. Bowers*, 15 Fed. (2d) 287 involved an agreement between husband and wife whereby the latter should "be entitled to one-half *of the profits* which shall come to the party of the first part from said firm" (9 Fed. (2d) 415) and furthermore the contract might "be terminated by either party at any time": as stated by the Circuit Court of Appeals in its opinion (15 Fed. (2d) 289): "* * * in any view the provision which allowed him *at his pleasure* to denounce the agreement put the absolute disposition of the profits always within his power." The court distinctly indicated that its decision would have been for the taxpayer had his wife acquired by the agreement any interest legal or *equitable* in the firm assets.

That Mrs. Leininger acquired by the agreement of 1920 either a legal or an equitable interest in the firm assets is clear from a long line of authority *inter alia*:—

Smith-Powers Logging Co. et al. v. Bernitt et al., 237 Fed. 570, 572;
30 *Cyc.* 605;
Meaher v. Cox, 37 Ala. 201;
Rosenstiel v. Gray, 112 Ill. 282;
Harvey v. Ford, 83 Mich. 506;
Nixon et al. v. Nash et al., 12 O. S. 647;
Parish v. Bainum et al., 306 Ill. 618;
Sherk v. First National Bank, 152 S. W. 832;
Day v. Stafford, 107 S. W. 433;
Beecher v. Stevens et al., 43 Conn. 587;
Home State Bank v. Vandolak et al., 188 Ill. A. 123;
Stokes et al. v. Stevens et al., 40 Cal. 391.

In this connection attention is called to the finding (R. 20) that the partners of Mr. Leininger were informed in 1920 of "the fact of this transfer" and that the business continued without protest or further change at least through the tax years here involved, i.e., 1920-1923 inclusive, from which, unquestionably, acquiescence must be inferred as a matter of fact and law. (*Rosenstiel v. Gray* and *Smith-Powers v. Bernitt, supra.*)

Harris v. Commissioner, 39 Fed. (2d) 546, cited by petitioner, was decided directly on the authority of *Mitchel v. Bowers* and, as indicated by the syllabus, involved merely an "assignment of interest *in profits.*" In fact, the Circuit Court of Appeals for the Second Circuit itself clearly defined the intended scope of the cases now cited by petitioner when it said in *Commissioner v. Marshall Field*, 42 Fed. (2d) 820, 822:

> "These (*Mitchel v. Bowers, supra, Harris v. Commissioner, supra,* and *Lucas v. Earl, infra*) were, however, all cases in which, though the instrument affected to convey an existing interest in property, there was none at the time which the law recognized. We do not understand that where there are such, they may not be assigned like other property, or that when they have been, the income is still taxable to the assignor."

To conclude this branch of the discussion we call attention to *Hellman v. United States*, 44 Fed. (2d) 83, wherein the Court of Claims on rehearing reversed a previous decision and held:

> "Defendant contends * * * that plaintiff was bound by the partnership return showing his distributive share * * * Partners may adjust between themselves their distributive share in such proportion and in such manner as they may desire. * * * Bookkeeping entries do not constitute income *unless there is the right of* ownership in the amount disclosed by such entries."

And to a long line of Board and Court cases which condemn the theory urged by petitioner when applied to facts such as those found herein. Typical of such cases is *Wing v. Commissioner,* 17 B. T. A. 1028, wherein the Board said:

> "In this theory it has been overlooked that the identity of the party taxable upon income from a partnership interest is not determined merely by the name in which such interest is held but by the ownership of the corpus of the partnership interest.
>
> "As we view it, the income received by petitioner's wife upon her actual interest in the assets producing such income represented income to her whether she was in law a partner or whether the partnership agreement was under state law inoperative to create as to her a partnership liability. It is clear that even had petitioner's wife not been a party to the contract of partnership and the amount here in controversy been paid to petitioner as a portion of the distributive income of a partnership interest standing in his name alone, he would have received this sum merely as a trustee for her, to whom it would be taxable."

It is noteworthy that the Commissioner formally "acquiesced" in the last cited decision, as did he also in the decision in *Hallahan v. Commissioner,* 14 B. T. A. 584, wherein at page 596 the Board said:

> "Can it be said, merely because they are profits upon a partnership interest standing in petitioner's name, that they are distributable to him and must be included in the net personal income upon which he individually must pay a tax? We have had substantially this same situation presented to us before and have drawn definitely the distinction between these cases of which Ormsby McKnight Mitchel (*Mitchel v. Bowers, supra*) is an example, where the beneficial interest in the income alone has been assigned by the party owning the corpus, and those in which the income is produced by property belonging to two jointly, although the ownership of only one was disclosed and the total

income actually collected by that party, who then accounted to his undisclosed co-partner in interest for the latter's share. In these cases we have held the individual receiving the total income taxable only on the portion in which he individually had the beneficial interest, the portion paid his associate being merely received by him in trust for such party."

Commissioner v. Barnes, 30 Fed. (2d) 289 C. C. A. 3rd;
Parshall v. Commissioner, 7 B. T. A. 318, 321;
Thomas v. Commissioner, 8 B. T. A. 118, 119;
Kier v. Commissioner, 15 B. T. A. 1114, 1117-8;
Hinshaw v. Commissioner, 16 B. T. A. 1236;
Copland v. Commissioner, 41 Fed. (2nd), 501 C. C. A. 7th;
Dickinson v. Commissioner, 23 B. T. A. 1211.

2. The second reason urged for certiorari has already been sufficiently answered above. The findings in the instant case establish that the respondent assigned to his wife—not income alone when and as received—but corpus—namely an interest in his partnership interest—from which the income flowed. And *Bing v. Bowers*, 26 Fed. (2d) 1017, cited by petitioner in this connection, not only specifically points out and recognizes the distinction for which we contend, but also upholds

> "a gift or assignment to members of one's family * * * even though it be for the purpose of cutting down total family income tax * * * as long as the gift or assignment is actual or bona fide" (22 Fed. (2d) 450)

provided the assignment is one of income-producing corpus and not one of future income alone.

3. The decision in the instant case does not at all conflict with the holding of this Court in *Lucas v. Earl*, 281 U. S. 111. The income involved in *Lucas v. Earl* was salary

and fees earned by Earl: no part of the income involved therein consisted of profits or gains resulting or springing from capital, which latter are taxable solely to the person equitably owning the corpus or interest from which the earnings flowed. This Court in *Lucas v. Earl* aptly said with reference to the income involved therein:

> "That seems to us the import of the statute before us and we think that no distinction can be taken according to the motives leading to the arrangement by which the fruits are attributed to a different tree from that on which they grew."

Applying this comment to the instant case, obviously the share of profits paid to petitioner's wife was the "fruit" of her interest in the partnership—whether legal or equitable—and, therefore, taxable only to her. There is no analogy between profits so resulting from the ownership of capital and salaries or fees (as in *Lucas v. Earl*) which latter can flow solely from the personal services of the husband in which the wife could have no participating ownership. Indeed this Court in *Poe v. Seaborn,* 282 U. S. 101, pointed out, as already herein set forth, that the very language of the taxing statute indicates that an individual should be taxed only on income of which he has the "ownership," and, further, said:

> "In the *Earl* case * * * we held that * * * the husband's professional fees, earned in years subsequent to the date of the contract, were his individual income * * *. The very assignment in that case was bottomed on the fact that the earnings would be the husband's property, else there would have been nothing on which it could operate."

4. The Government's theory is, we believe, of the type which Mr. Justice Sutherland had in mind in *Lynch v. Alworth,* 267 U. S. 364, when he said:

> "And the plain, obvious and rational meaning of a statute is always to be preferred to any curious, nar-

row, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."

We submit that the peculiar facts (referring especially to the Board's findings) render the question involved herein one of very limited application to other taxpayers. The decision below, upon the facts, is in complete accord with the decisions of this and other courts. To sustain the petitioner's position would be to ignore the definition of income laid down by this Court in *Eisner v. Macomber* (*supra*). Section 213 (a)* of the Revenue Acts of 1918 and 1921, in defining income, speaks of "gains, profits and income * * * growing out of the ownership of * * * property." Clearly the income here in question grew out of property owned by the respondent's wife and was, therefore, her and not his taxable income. Whether the basic agreement as found by the Board, coupled with the knowledge and acquiescence of the other partners, constituted respondent's wife a member of the principal partnership or merely the equitable owner of a half interest in the respondent's interest therein, seems immaterial; on either hypothesis the income allocable to her interest, to paraphrase the words of this Court in *Lucas v. Earl,* was "fruit" which "grew" upon a tree of which she was the owner.

It is respectfully submitted that the decision below upon the specific facts as found is in complete accord with the law as heretofore announced by this Court as well as by the various Circuit Courts of Appeals that have passed upon the question; and that the writ should therefore be denied.

LEVI COOKE,
GEORGE R. BENEMAN,
IRWIN N. LOESER,
Counsel for Respondent.

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*See Appendix.

APPENDIX.

Section 213:

(a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period.

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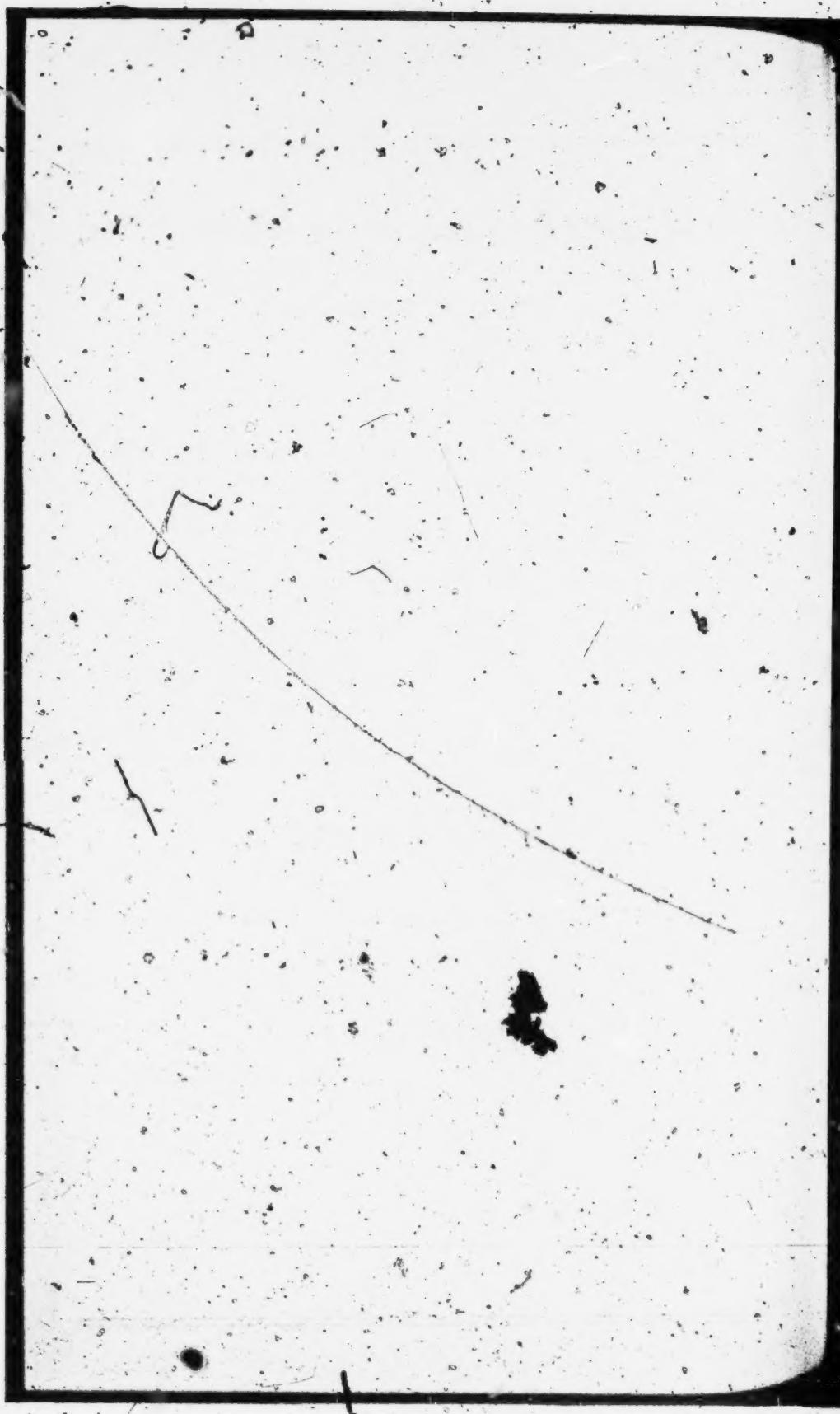

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BRIEF FOR RESPONDENT.

QUESTION PRESENTED.

The sole issue may, we believe, be fairly stated as follows:

> "A, resident and citizen of Ohio, being in partnership with B, each owning a half interest, entered into an agreement with his wife W, based upon a legally sufficient consideration, whereby W became 'a full equal partner' with A in his 'interest' in the partnership; 'the fact of the transfer was communicated' to B. The business continued without objection or interruption. Under these circumstances is A to be taxed upon all of the subsequent profits attributable to the one-half interest originally owned by him, or may A and W each return and pay tax upon one-half thereof?"

STATUTES INVOLVED.

These are set forth in the Appendix of Petitioner's Brief, pp. 29-32.

STATEMENT.

The peculiar and special facts of the case are set forth in the findings of the United States Board of Tax Appeals, which we summarize as follows:

1. "In 1898 a partnership known as Eagle Laundry Company was" formed by respondent "and one M. G. Monaghan, each owning a one-half interest." (R. 16)

2. "In 1904 Monaghan died and his wife, Mary T. Monaghan, succeeded to his interest in the firm and on the books of the company." (R. 16)

3. "In 1920 Mary T. Monaghan transferred by bill of sale her interest to her children. The entire Monaghan interest was thereafter carried on the books in the name of Marcus A. Monaghan." (R. 16) * * * "Each of the three children of Mary T. Monaghan, however, returned a proportionate part of the income for taxation." (R. 16)

4. "During the latter part of 1920 a written agreement, confirmatory of a pre-existing oral agreement, was entered into between petitioner[1] and his wife, wherein it was acknowledged that *petitioner's wife had been and was a full equal partner* with him *in the interest* in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses. The contract was effective from the beginning of 1920." (R. 17)

---

[1] "Petitioner" before the United States Board of Tax Appeal is the Respondent herein.

Note: All italics throughout this brief are supplied.

Note: The United States Board of Tax Appeals is sometimes hereinafter referred to as the "Board".

5. "The fact of this transfer was communicated to Marcus A. Monaghan, who represented the owners of the other one-half interest in the Eagle Laundry Company." (R. 17)

6. "The Leininger interest always stood in the name of C. P. Leininger on the partnership books but Mrs. C. P. Leininger returned one-half of the profits of the Leininger interest for taxation." (R. 17)

7. "Petitioner[1] and his wife maintained prior to and throughout the period here involved a joint bank account on which each could draw unrestrictedly. The profits received from the partnership were deposited in this account by Leininger, no checks on the partnership being drawn to the wife." (R. 17)

SUMMARY OF ARGUMENT.

The trial court, namely the United States Board of Tax Appeals, having made findings of fact, those findings must here be given the same effect as a jury's verdict. The Board found as a fact that the "interest" of the respondent in the partnership was, with the knowledge of the respondent's partners, owned in equal shares by himself and his wife. It follows as a necessary conclusion of law that the profits of the partnership allocable to the wife's "interest" in the respondent's "interest" were taxable income to her and not to him. The 1920 agreement referred to in the Board's findings assigned to her not merely future earnings but rather a portion of the corpus from which those earnings were to flow. As said by the Circuit Court of Appeals in its opinion (R. 26):

> "We cannot regard this contract as a mere assignment of an interest in future profits 'if, when and as' received. It creates mutual rights and liabilities; it is irrevocable; it creates, at least as between the parties, a vested interest in a property right; and the specified profits and losses were hers, not his."

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[1] See footnote, page 2.

The contract between respondent and his wife was upon a legally sufficient consideration; it was a lawful and binding agreement. The parties were competent to make such contract under the law of Ohio. The agreement, having been entered into in good faith, must be recognized and sustained even though the result may be to lessen the aggregate income tax liability of husband and wife. The benefit so derived, if any, was procured by the respondent at the cost of a conveyance (found by the Board as a fact) to another of a one-half interest in his interest in the partnership. That conveyance, *concluded and irrevocable,* even though made to his wife, might be to his decided disadvantage in the future, for it gave the wife with the knowledge of his partners full right of ownership, whether legal or equitable is immaterial, in an existing corpus; such ownership importing *inter alia* ownership in her own right of income consequent upon her share in the corpus. They made the agreement for better or for worse and should be permitted to harvest its advantages while being held to its burdens.

We shall endeavor to make clear that the judgment of the Court below upon the facts as found, is correct—this case, under its own special facts, being easily distinguishable from the authorities upon which the Government relies—the latter being cases in which the assignment amounted to no more than an attempt to transfer future income as such with no concurrent transfer *in praesenti* of the corpus producing such income. The applicable sections of the Revenue Acts of 1918 and 1921, the decisions of the Board of Tax Appeals, those of the several Circuit Courts of Appeal and of this Court, fully recognize the distinction for which we contend. The rule which runs through all the cases, as we shall show, was, perhaps, well stated by the Board in *J. V. Leydig v. Commissioner,* 15 B. T. A. 124, 132 (affirmed 43 Fed. (2d) 494 C. C. A. 10 and ac-

quiesced in by the Commissioner of Internal Revenue in C. B. VIII-2 page 31) as follows:

> "The cases * * * are singularly free from conflict as to the principle governing the issue raised. From them we conceive the rule to be that income *per se* cannot be assigned to relieve the assignor of the tax levy, but, where the thing assigned was a property right, real or personal, productive of income, income thereafter arising from such property is income to the assignee by virtue of his ownership."

We shall present our argument and citations under five headnotes, as follows:

I. The United States Board of Tax Appeals found as a fact that respondent's wife owned the corpus which produced the income here in issue: the findings of fact made by the Board are, for the purposes of this case, conclusive.

II. Income is taxable only to the equitable owner of the corpus which produces such income.

III. Section 218(a) of the Revenue Acts of 1918 and 1921 merely prescribes that partnership income is taxable directly to its owners whether distributed or or not. The word "partner" is used as synonymous with "owner". The rule heretofore discussed applies where the assigned corpus is part of a partnership interest.

IV. The construction of section 218(a) of the Revenue Acts of 1918 and 1921 urged by petitioner is unconstitutional.

V. The cases relied upon by the commissioner are based on facts readily distinguishable from those of the instant case: they apply to attempted assignments of future income only (as distinguished from an assignment of corpus as herein) or to revocable grants (as distinguished from an irrevocable assignment of corpus as found herein).

ARGUMENT.

I.

THE UNITED STATES BOARD OF TAX APPEALS FOUND AS A FACT THAT RESPONDENT'S WIFE OWNED THE CORPUS WHICH PRODUCED THE INCOME HERE IN ISSUE: THE FINDINGS OF FACT MADE BY THE BOARD ARE, FOR THE PURPOSES OF THIS CASE, CONCLUSIVE.

It should be observed that the evidence before the Board is not included in the record; upon the evidence the Board made special findings (R. 16, 17). These must be given "the same effect as the verdict of a jury" (28 U. S. C. A. 773, U. S. Rev. St. section 649) and, in the absence of a bill of exceptions containing the evidence, are conclusive. (*Cyc. of Federal Procedure*—Longsdorf—Volume VI, page 643). This rule is applicable to reviews of decisions of the Board of Tax Appeals (*Phillips v. Commissioner*, 283 U. S. 589, 600): as said by the Circuit Court of Appeals (6th) in *Cogar v. Commissioner*, 44 Fed. (2d) 554, 556

> "Upon this point the Board made a specific finding * * * none of the evidence before the Board of Tax Appeals is returned with the record and we cannot therefore review the question";

and by the Court of Appeals of the District of Columbia in *Evergreen Cemetery Association v. Burnet*, 45 Fed. (2d) 667

> "The record does not set out any of the testimony heard by the Board; the findings of fact reported by the Board are therefore accepted as conclusive";

see also *United States v. Copper Queen Mining Co.*, 185 U. S. 495, 497.

It should be noted from the Board's findings (R. 17) that, although on the partnership books the "Leininger interest" stood in respondent's name, his wife, "had been

and was a full equal partner with him in the interest"; also that the Monaghan interest in the partnership was "carried on the books in the name of Marcus A. Monaghan" (R. 16, 17) although *owned* by the three children of Mary T. Monaghan: in other words, the books disclosed as to both sides of the partnership a record ownership differing from the actual and equitable ownership; also "the fact" of the "transfer" of one-half of the Leininger interest to his wife "was communicated to Marcus A. Monaghan, who represented the owners of the other one-half interest." (R. 17) That the Board intended these findings to imply an ownership *in praesenti* of income-producing corpus rather than merely an assignment of future income is indicated by the inclusion in the Board's syllabus of the following language (19 B. T. A. 621): "Notwithstanding a contract beween himself and wife that they were partners in all of his property * * *." The petitioner in his brief (p. 4) concedes: "The evidence is not reported in the record, and the findings of the Board are not challenged."

The agreement found by the Board conveyed to respondent's wife a half ownership in a producing corpus. There is no restriction in Ohio against the full right of husband and wife to contract with each other as the Board found they had. (*Bank v. Rice*, 22 O. C. C. 183, 198; *Dillingham v. Dillingham*, 28 O. C. A. 49, 60, 61; *Gould v. Cooper*, 15 O. A. R. 223; *Dredge and Dock Co. v. Smith*, 16 O. C. C. N. S. 344, affirmed 84 O. S. 482; *Higbee Co. v. Crum*, 27 O. A. R. 107; *Shafer v. Shafer*, 30 O. A. R. 298, 299.)

Section 7999 General Code of Ohio provides:

> "A husband or wife may enter into any engagement or transaction with the other, or with any other person, which either might if unmarried;"

Bearing in mind the knowledge of each of the record partners as to the subdivision of the interest of the other (R. 17) the conclusion is inescapable that Mrs. Leininger became, by virtue of the agreement as found, either a member of the original partnership (*Rosenstiel v. Gray*, 112 Ill. 282; *Smith-Powers Logging Co. et al. v. Bernitt, et al.*, 237 Fed. 570, 572) or, at least, the equitable half owner of the Leininger interest (*Nirdlinger v. Bernheimer*, 133 N. Y. 45, 53; *Nixon and Chatfield v. Nash, et al.*, 12 O. S. 647, 649; *Parish v. Bainum et al.*, 306 Ill. 618). As said in *Sherk v. First National Bank* (Texas), 152 S. W. 832: "A partner's 'interest' is property which can be sold and transferred" and the assignee becomes "a tenant in common with the co-partner" (*Stokes, et al. v. Stevens, et al.*, 40 Cal. 391, 394); or, as held in *Van Brocklen v. Smeallie*, 140 N. Y. 70, "plaintiff's partnership interest was personal property, and the title passed at once on the execution of the agreement."

We submit that a serious fallacy runs through the petitioner's brief in that it ignores the express findings of fact made by the Board. We refer particularly to the findings:

> (1) That the agreement between respondent and his wife recognized her as "a full equal partner with him in the interest in The Eagle Laundry Company" (R. 17);
>
> (2) That "the fact of this transfer was communicated" to the representative of the other partners (R. 17).

Notwithstanding these findings the petitioner argues that respondent's wife, by the agreement, acquired only a right to receive a share of profits when and as earned, that she became neither a partner in the laundry company nor the owner of the corpus which produced the income here in

question. We may summarize and briefly answer the arguments so made as follows:

(1) That the "other partners" did not *expressly* consent. The petitioner in his brief (p. 6) refers to the "other partners" thereby conceding that the Monaghan children had all become partners by virtue of the bill of sale referred to at R. 16. "The fact" of the transfer by respondent to his wife was communicated to the representative of "the owners of the other half interest" (R. 17). And, as the petitioner admits in his brief (p. 27), "the business of the laundry company continued thereafter as it had before." Obviously there was acquiescence by the "other partners" to the entry of Mrs. Leininger into the partnership. Petitioner argues that the injection of a new member operates as a dissolution. But laymen do not give thought to such legal niceties; and, in any event, if there was a technical dissolution of the old, there occurred instantly the formation of a new partnership with Mrs. Leininger as a member, in the same manner as the children of Mrs. Monaghan had become members by virtue of the bill of sale (R. 16). The case, we submit, is on all fours with *Smith-Powers Logging Company et al. v. Bernitt et al.*, 237 Fed. 570, 572.

(2) Next the Petitioner argues that the absence of Mrs. Leininger's name in the books and tax returns of the partnership precludes her being treated as a partner. But tax liability is not to be determined by "mere book entries"; it must stand upon the solid ground of intent and fact, where such intent and fact can be found, as they were specifically found by the Board in the instant case. As was said in *Eaton v. English and Mersick*, 7 Fed. (2) 54:

> "We are not particularly concerned about the entries which were made in the books of the company. We may repeat what we said in *Douglas v. Edwards*, 298 Fed. 229, 234, that it is well to realize that, in this case, the rights of the parties can neither be

established nor impaired by the bookkeeping methods employed or by the names given to the various items."

As this Court said in *Doyle v. Mitchell*, 247 U. S. 179, 187, the facts and not the book entries govern. (See also *Isbell Porter v. Commissioner*, 40 Fed. (2) 432; *A. Kreamer Inc. v. U. S.*, 66 Ct. Cl. 308; *Henry Myer Thread Mfg. Co. v. Commissioner*, 2 B. T. A. 665, 666; *Appeal of Cleveland Woolen Mills*, 8 B. T. A. 49.)

(3) The petitioner further urges that Mrs. Leininger "did not possess other powers which ordinarily or necessarily inhere in a partner." But, we may answer, there are various classes of partners; Mrs. Leininger may well have been a secret, a silent or a dormant partner (47 *C. J.* 647, 713) and yet a partner as far as this cause is concerned.

(4) Equally without force is the suggestion that the respondent's wife contributed no capital to the partnership. Contribution of either capital or services is not essential (20 *R. C. L.* 834). But if a contribution to capital were necessary, it must be conceded by petitioner that from 1920, at least, Mrs. Leininger was an equal owner of the respondent's investment and the leaving of that interest in the business constituted her capital contribution thereto.

(5) The argument that there was a failure to file a certificate setting forth Mrs. Leininger's interest in the partnership, as required by Ohio General Code Sections 8099, 8102 is devoid of merit. Those sections do not have the effect apparently assumed by counsel. They are followed by Section 8104 which fixes the penalty for noncompliance in the form of a merely temporary stay to actions on contracts brought by the partnership; the sections in question do not in any degree affect the validity of a partnership or the rights of partners. (47 *C. J.* 746; *Commissioner v. Barnes' Estate*, 30 F. (2) 289.)

(6) Finally, the argument is made, "Even if this Court should hold that taxability of the partnership income

always follows the ownership of the income-producing corpus the respondent must fail. For here that corpus consisted of the physical assets and intangible assets of the company. To the extent that these elements of a going business could be owned, they belonged to the partners of the Eagle Laundry Company as joint owners."

We respectfully submit that the income-producing corpus, so far as the Leininger income was concerned, was not the physical assets as such of the partnership, for the title thereto was in the partnership and not in the partners (see *infra*), but rather the partnership interest of the respondent, which partnership interest was transferable as a matter of law and was (as to one moiety) transferred as a matter of fact by respondent to his wife. There is no thought on our part that the mere right to share profits constitutes one a partner or that a mere transfer of a right to receive future profits relieves the assignor of the tax burden. But Mrs. Leininger became not merely a sharer of profits and losses; by the very terms of the Board's findings (R. 17) she was *"a full equal partner with him in the interest in the Eagle Laundry Company."* It is true that the finding recites that she was "entitled to share equally in the profits and obligated to bear equally any losses" but the use of that clause does not detract from the import of the finding of "full equal" partnership. The maxim *"Expressio eorum quae tacite insunt nihil operatur"* applies. (See *Broom "Legal Maxims"*, 3rd ed. p. 424.) Clearly respondent's wife was constituted the owner not alone of future profits but, over and beyond that, the owner of something more fundamental, namely of an interest in the business itself. To make it unequivocal and emphatic the Board used the expression, as had the contract, "full equal partner."

> "Although no partner owns absolutely any part of the property, he has his own interest in the whole; which interest we have defined as an ownership of the

whole, subject to the ownership of the other partners. And the question has repeatedly arisen, whether he can sell and transfer this interest. The answer, in general, is in the affirmative." *Parsons on Partnership* (4th ed. Section 112).

"Thus it may be stated that each member of the firm has an interest in the firm property which is hardly more than a chose in action, an interest somewhat uncertain in its value, subject to levy * * * to his mortgage * * * and to sale by him either to a copartner or a third person * * * it must be considered property." *Rowley "Modern Law of Partnership,"* Sections 291, 292.

"It is immaterial what effect the assignment by C of his interest in the property belonging to the firm of C and H had upon the partnership, or whether the assignee and H constituted a new partnership. The assignment, at least, operated to vest C's interest in the assignee, and to make him, jointly with the other partner, the owner of the assets which had belonged to the partnership." *Keith & Son v. Ham,* 89 Ala. 590, 593.

See also *Stokes et al. v. Stevens,* 40 Cal. 391.

The transferee of a partner's interest gets not specific assets as such because his grantor had no such title to convey: "the property or effects of a partnership belong to the firm and not to the partners"; but the transferee acquires exactly what the grantor had to convey, namely "a partnership interest." (*Bank v. Carrollton Railroad,* 78 U. S. 624, 628, 629.)

We submit that the entire substructure of petitioner's argument falls and the cases relied upon become inapplicable when we apply to the findings of fact in the instant case the words of the court in *Rosenstiel v. Gray,* 112 Ill. 282 cited with approval by the Circuit Court of Appeals (9th) in *Smith-Powers v. Bernitt* (*supra*). At p. 291 the court said:

"From the length of time which elapsed * * * with no objection appearing * * * there would be ground of inference of an implied acquiescence * * * in R's becoming a member of the firm. *But, supposing R was not a partner* with the consent of Rosenstiel, *he was a joint owner* with G, S and Rosenstiel at the time Rosenstiel went out of the firm * * *."

And so, we contend, there is no warrant for the assumption by the petitioner in this case that the agreement between respondent and his wife amounted only to an attempted transfer of future profits. The findings of fact vitiate such assumption. Whether the agreement, coupled with the knowledge and acquiescence (as found by the Board) of the other partners, was tantamount to the admission of the respondent's wife into the partnership or merely constituted her a joint owner with him of his interest therein, the Board's findings compel the legal conclusion that, by virtue of the agreement, during the years involved, the respondent's wife was the owner *in praesenti* of a fixed, definite property corpus, and that corpus was the source of the income here involved. The supposed difficulty conjured up by the petitioner at page 10 of his brief is no difficulty at all; the wife would stand precisely in the shoes of the husband as to the interest acquired by her, taxable under the same conditions, at the same time and to the same extent as he.

II.

INCOME IS TAXABLE ONLY TO THE EQUITABLE OWNER OF THE CORPUS WHICH PRODUCES SUCH INCOME.

As we shall see, the cases upon which the Government relies involve only an assignment or attempted assignment of income *in futuro*. Such cases have no application to the facts of the instant case as found by the Board. For example, two cases most strongly urged by the Government

as in conflict with the decision of the Circuit Court of Appeals herein, namely *Mitchel v. Bowers,* 15 Fed. (2d) 287 and *Bing v. Bowers,* 26 Fed. (2d) 1017, distinctly recognize the correctness of our position under the facts of the instant case.

The syllabus of *Mitchel v. Bowers* (*supra*) indicates that the Court's judgment would have been for the taxpayer had his wife acquired by the operative agreement a "present interest equitable or legal." And in *Bing v. Bowers* (*supra*) the Court of Appeals, Second Circuit, affirmed "upon the opinion of Mack, *J.*, below" *Bing v. Bowers,* 22 Fed. (2d) 450, wherein the distinction between a mere assignment of future income and the transfer of an interest in income-producing corpus is set forth at great length and with compelling logic. The propositions of the syllabus of *Bing v. Bowers* indicate conclusively that the judgment below *does not conflict* with either *Mitchel v. Bowers* or *Bing v. Bowers* (*supra*):

> 1. "A gift or assignment to members of one's family is proper, even though it be for the purpose of cutting down total family income tax contribution to the government, as long as the gift or assignment is actual or bona fide."
>
> 5. "Where instrument executed by son assigned to mother certain so-called annuities, payable out of income from interest in property, *did not pass his interest* or create a rent charge, *or any ownership pro tanto* of his interest in property, and grantee was at best only entitled to net income or to stipulated sums to be paid therefrom, and grantor maintained right of control, the income received therefrom was taxable to grantor, notwithstanding the instrument was *in form* proper for a grant of interest in real estate."
>
> 6. "Where assignor of future income from property *remains the owner* thereof, the income therefrom is taxable to him as fully as when he grants it as a gift in advance of his receipt, as it clearly is, despite a gift thereof immediately after its receipt."

Indeed the Court of Appeals for the Second Circuit, which had decided the cases of *Mitchel v. Bowers, Bing v. Bowers* and other cases cited herein by the Government, itself clearly defined the intended scope and limitations of these cases by holding, in *Commissioner v. Marshall Field,* 42 Fed. (2d) 820, 822:

> "These were, however, all cases in which, though the instrument affected to convey an existing interest in property, there was none at the time which the law recognized. We do not understand that where there are such, they may not be assigned like other property, or that, when they have been, the income is still taxable to the assignor."

The United States Board of Tax Appeals, as we have already seen in our reference to the *Leydig* case (*supra*), has recognized and followed the rule for which we contend. The difficulty the Board has had, as evidenced by its decisions, has been, not as to the validity of the rule, but rather as to the legal implications of the facts of each case as presented. For example, in *Copland v. Commissioner,* 15 B. T. A. 238, there was involved the question as to whether the Petitioner had conveyed to his wife his interest in a joint venture or merely his share of the profits thereof when and if earned. The Board held against the Petitioner on the facts, but said, at page 240:

> "If the asset giving rise to the income was assigned, then the income is not taxable to the petitioner. But if income or profits only were assigned, they become taxable to the petitioner regardless of their assignment or transfer to the petitioner's wife."

The Circuit Court of Appeals (7th), on review, reversed (41 Fed. (2d) 501) and said at page 504:

> "Appellee has called our attention to *Rosenwald v. Commissioner,* 33 F. (2) 423 and *Bing v. Bowers,* 22 F. (2) 450, as determinative of the question of transferring without consideration a thing not in existence.

In these cases the donor never parted with possession and control of the corpus; in the instant case he did, and the transfer included more than future profits—it included not only the right to draw the profits, but *the very thing which would produce them.* • • •

"It is further contended by appellee that the future profits of the venture were not assignable, for the reason that they were not then in existence. The instrument in controversy not only assigns to his wife all of petitioner's right, title and interest in and to any profits, issues and income that may arise thereunder, but also all of his right, title and interest in and to the syndicate agreement. *This assignment includes more than future income—it includes the thing that produces the income, and the right to receive the income.*"

In *Parshall v. Commissioner,* 7 B. T. A. 318, the Board, after stating the Commissioner's reliance upon *Mitchel v. Bowers* (*supra*) said, at page 321:

"The question involved in that case was very substantially different from the question at issue in the instant case. In the *Mitchel* case the husband was a partner in a firm. He made a contract with his wife by which he agreed for a valuable consideration to transfer and assign to her, until future notice, one-half of his share of the profits of that partnership. *There was no attempt on his part to convey to his wife his interest in the partnership or any part thereof. She received no vested right* or interest in the partnership as such. All she received was a right to demand from him one-half of the profits he received from that business."

And, in a case almost identical with the case at Bar, namely *Thomas v. Commissioner,* 8 B. T. A. 118, the Board held, as syllabus:

"A member of a partnership is not individually taxable on so much of the partnership income as is *attributable to an interest in his interest* in the part-

nership which, at the date of the formation of the partnership, he had sold to a third person although such purchaser was not a member of the partnership."

And in its opinion, at page 119, the Board said:

"The transaction between petitioner and his daughter * * * was a sale of capital assets. * * * The daughter purchased not an interest in profits alone, but a one-half interest in petitioner's one-half interest in R. P. Drilling Company. * * * As between her and petitioner there existed *a partnership not only as to profits but also as to corpus.* If petitioner had defaulted on his contract, the daughter would have been entitled to bring an action against him and in that action to have made Parks a party for the purpose of an accounting. See *Nirdlinger v. Bernheimer,* 133 N. Y. 45. Petitioner held his daughter's interest in trust for her. Cf. *Barnes v. Alexander,* 232 U. S. 117. * * *.

"This income was, as to her, taxable income and as such has been properly returned and taxed. This income which was taxable to the daughter was not, under the facts of this case, at the same time taxable also to the petitioner. He held it as trustee, and since it was at once distributable, he had the right under section 219 of the Revenue Act of 1918 to deduct it from the gross income of the trust.

"This conclusion is not in conflict with the decisions in *Appeal of S. V. Woods,* 5 B. T. A. 413; *Appeal of Fred W. Warner,* 5 B. T. A. 963; *Appeal of Ormsby McKnight Mitchel,* 1 B. T. A. 143; and *Mitchel v. Bowers,* 15 Fed. (2) 287. In each of these cases the transaction involved was the transfer to another of income which arose from the property of the transferor and in each case it was held that such transfer did not lessen the taxable income of the owner of the property from which the income was derived. In this case petitioner did not assign income produced or to be produced from his property. He sold an interest in his interest in the Drilling Company. It was his daughter's interest in the corpus which produced her share of the

income. The *Mitchel* case contained another important element which is not present in this case. The contract between Mitchel and his wife was revocable by either party."

And in *Hallahan v. Commissioner*, 14 B. T. A. 584, involving income arising upon a partnership interest standing on the books in the name of one but equitably owned by others, the Board said at page 596:

> "This petitioner under the rule stated, is, as to the interests of his mother and brother in the partnership interest passing to him on his father's death, merely a trustee and any profits distributed to him are received in trust to the extent of their interests, just as any other income of trust property is received. He has no beneficial interest in them.
>
> "Can it be said, *merely because they are profits upon a partnership interest standing in petitioner's name,* that they are distributable to him and must be included in the net personal income upon which he individually must pay a tax? We have had substantially this same situation presented to us before and have drawn definitely *the distinction* between those cases of which *Ormsby McKnight Mitchel, supra,* is an example, where the beneficial interest in the *income alone* has been assigned by the party owning the corpus, and those in which the income is produced by property belonging to two jointly, *although the ownership of only one was disclosed* and the total income actually collected by that party, who then accounted to his undisclosed co-partner in interest for the latter's share. In these cases we have held the individual receiving the total income *taxable only on the portion in which he individually had the beneficial interest,* the portion paid his associate being merely received by him in trust for such party. Citing *C. R. Thomas,* 8 B. T. A. 118; *W. W. Parshall,* 7 B. T. A. 318; *Ralph L. Hinckley,* 6 B. T. A. 312; *H. P. Kelly,* 9 B. T. A. 832."

It seems obvious from the foregoing that the Board's decision herein (which the Circuit Court of Appeals

reversed) was in direct conflict with its decisions in other cases upon comparable facts; that the reversal of the Board by the unanimous decision of the Circuit Court of Appeals was proper and, upon the facts, there is no conflict between that decision and the holding of the Court of Appeals in the Second Circuit in *Mitchel v. Bowers* and other cases (*supra*).

III.

SECTION 218(a) OF THE REVENUE ACTS OF 1918 AND 1921 MERELY PRESCRIBES THAT PARTNERSHIP INCOME IS TAXABLE DIRECTLY TO ITS OWNERS WHETHER DISTRIBUTED OR NOT. THE WORD "PARTNER" IS USED AS SYNONYMOUS WITH "OWNER". THE RULE HERETOFORE DISCUSSED APPLIES WHERE THE ASSIGNED CORPUS IS PART OF A PARTNERSHIP INTEREST.

Section 218(a) of the Revenue Act, so far as here material, provides:

> "Section 218(a). That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner *his* distributive share, whether distributed or not, of the net income of the partnership for the taxable year. * * *"

It is apparently the Government's present claim that there is something so inherently peculiar in a partnership interest that the record partner must be taxed upon all profits attributable to his record interest even though another may be the legal or equitable owner of that interest in whole or in part. That such is not the law has been repeatedly decided. In fact in *Hallahan v. Commissioner* (*supra*) the Board expressly repudiated this idea and *the Commissioner acquiesced in the decision* (VIII-2 C. B. 21). The decision of the Board in *Thomas v. Commissioner*

(supra) was to the same effect. And in *Wing v. Commissioner*, 17 B. T. A. 1028 (acquiesced in by the Commissioner, IX.—1 C. B. 59), the Board

> "Held, that the beneficial ownership of a one-sixth interest in the partnership property being in petitioner's wife, the one-sixth of the earnings of the partnership paid her individually by it represented income to her and not to petitioner."

Approving its position in the *Thomas* case *(supra)* and in many other cases cited in the opinion, the Board said, in the *Wing* case (at page 1030):

> "In this theory it has been overlooked that the identity of the party taxable upon income from a partnership interest is not determined merely by the name in which such interest is held but by the ownership of the corpus of the partnership interest.
>
> "As we view it, the income received by petitioner's wife upon her actual interest in the assets producing such income represented income to her whether she was in law a partner or whether the partnership agreement was under state law inoperative to create, as to her, a partnership liability. It is clear that even had petitioner's wife not been a party to the contract of partnership and the amount here in controversy been paid to petitioner as a portion of the distributive income of a partnership interest standing in his name alone, he would have received this sum merely as trustee for her, to whom it would be taxable."

In *Rucker v. Blair*, 32 Fed. (2d) 222, the Circuit Court of Appeals Ninth Circuit had for decision the question whether partnership profits were taxable *in toto* to the record partners even though the interest of one of the partners had been acquired with "community" funds. The Court said at page 224:

> "There is no *alchemy* in the term 'partnership' or in the relation it imports, and contributions of community funds to a joint or partnership enterprise are

not *ipso facto* converted into separate property. We are concerned with the status of property invested, not with the form in which it was held."

The Court accordingly held as syllabus (page 222):

"Where partnership, engaged in real estate business, after marriage of partner entered into logging and sawmill business on borrowed capital, and it did not appear that capital was procured on credit of or for benefit of property owned by partnership at time of partner's marriage, partner's share of profits resulting from logging enterprise was community income * * * and partner was required to make individual tax return *for only one half of his distributive share* leaving other half to be taxed as wife's property under Revenue Act of 1926."

The Circuit Court of Appeals Third Circuit in *Commissioner v. Barnes' Estate,* 30 Fed. (2d) 289, had for review the Board case reported in 7 B. T. A. 924. There had been informalities in the attempted transfers from husbands to wives of the husbands' interests in a partnership. The Board stated the question (p. 926):

"There remains, however, the question of law whether or not in view of the facts in the case there was a legal transfer of the interest in the partnership, or a gift of the profits, as and when such profits flowed from the partnership to the men, themselves, as partners."

Both Board and Court held for the taxpayers, the syllabus of the Court's decision reading:

"Gift to married women of interest of their husbands in partnership, made without notice to third partner, not registered and not followed by participation of assignees in management of company, held not void, as to Commissioner of Internal Revenue, under Uniform Partnership and Partnership Registration Act (Pa. St. 1920 section 16596 *et seq.*: sections 16639, 16640) where assignees received profits as partners

and paid income tax and assignment was made in good faith."

It is of interest to note that the Board, in deciding the instant case, cited and relied on *Hellman vs. United States* (R. 21) Court of Claims May 2, 1927 A. F. T. R. 6781. The Government likewise in its briefs below. But the decision of the Court of Claims in the *Hellman* case so relied upon by the Board and the Government was subsequently reversed on new trial (44 Fed. (2d) 83) and by a unanimous court. In that case partners had readjusted among themselves their respective participations in profits on a basis differing from that shown in the principal partnership agreement, the books and the tax returns. The Court said, in the course of a long opinion (pp. 89, 90, 91):

> "A new trial was allowed in this case * * * Defendant contends * * * that plaintiff was bound by the partnership return showing his distributive share. * * * Partners may adjust between themselves their distributive share in such proportion and in such manner as they may desire * * * Bookkeeping entries do not constitute income unless there is the right of ownership in the amount disclosed by such entries."

Undoubtedly the court below was entirely right when it said in its opinion (R. 26): "We do not see that Section 218(a) undertakes to fix any policy as to who is to be deemed to receive the income; it merely extends the definition of individual income so as to include partnership profits," whether distributed or not.

We submit that the Sixteenth Amendment was not intended to authorize the taxation of one person on income flowing from corpus *owned* by another. It should be observed that Section 218(a) relied upon by the Government did not impose any tax. Section 210 imposed the tax on individuals in the following words:

"Section 210 * * * there shall be levied * * * upon the net income *of* every individual a * * * tax at the following rates * * *."

The sole purpose of Section 218(a) appears to have been to provide that partnerships as such should pay no tax, but rather that the tax payable by reason of the partnership income, whether distributed or not, should be paid by the owners of the business as individuals. To tax the respondent upon income arising from corpus in which he had no beneficial interest would run counter to the definition of taxable income long since settled by this Court in *Eisner v. Macomber,* 252 U. S. 189, 207 as being "gain * * * derived, that is, received or drawn by the recipient for his separate use, benefit and disposal." The definition of income so announced by this Court has been frequently reiterated. (*U. S. v. Phellis,* 257 U. S. 156, 169; *Taft v. Bowers,* 278 U. S. 481; *Poe v. Seaborn,* 282 U. S. 101.) In the last cited case this Court said (p. 109):

> "The case requires us to construe sections 210(a)[1] and 211(a) of the Revenue Act of 1926 and apply them, as construed, to the interests of husband and wife in community property under the law of Washington. These sections lay a tax upon the net income of every individual. The act goes no farther, and furnishes no other standard or definition of what constitutes an individual's income. *The use of the word 'of' denotes ownership.* It would be a strained construction which, in the absence of further definition by Congress, should impute a broader significance to the phrase."

As said by the Circuit Court of Appeals (8th) in *Central Life Society v. Commissioner,* 51 Fed. (2d) 939, 941:

> "Tax laws are essentially practical * * * and the federal income tax laws are no exception. While, for

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[1] The language has been the same in each act since that of February 24, 1919, 40 Stat. at L. 1057, Chap. 18 U. S. C. title 26 Section 1262.

purposes of convenience and certainty in collection of such taxes, it is sometimes provided that those who collect income for others shall pay therefrom the taxes thereon, yet a cardinal purpose of the income tax laws is to tax the income to the person who has the right or beneficial interest therein, and not to throw the burden upon a mere collector or conduit through whom or which the income passes." (Numerous citations)

See also *Pugh v. United States,* 48 Fed. (2d) 600; *McKee v. Alexander,* 48 Fed. (2d) 838.

We submit, therefore, upon this phase of the case that Section 218(a) uses the word "partner" as synonymous with, and with no other force and effect than, "owner"; that the use of the word "his" in conjunction with the words "distributive share" in said section implies "ownership" just as the word "of" used in Section 210 was held by this Court in *Poe v. Seaborn (supra)* to "denote ownership"; that, as said in *Rucker v. Blair (supra)* "there is no alchemy in the term 'partnership' * * * we are concerned with the status of property invested, not with the form in which it was held." It follows that the income here in question was taxable only to the respondent's wife, she being the owner of the property or corpus which produced that income.

IV.

THE CONSTRUCTION OF SECTION 218(a) OF THE REVENUE ACTS OF 1918 AND 1921 URGED BY PETITIONER IS UNCONSTITUTIONAL.

To assess income tax liability against respondent predicated upon profits accruing upon a partnership interest owned by his wife merely because Section 218(a) provides that "the net income of each partner" includes "his distributive share, whether distributed or not, of the net income of the partnership" would clearly run counter to the Fifth Amendment. *O'Malley-Keyes v.*

Eaton, 24 Fed. (2d) 436, 438. This infirmity in the Petitioner's position was suggested by the dissenting opinions of five members of the Board of Tax Appeals in *Battleson v. Commissioner*, 22 B. T. A. 455, wherein it was said (p. 465):

> "The Sixteenth Amendment to the Constitution never was intended to tax and does not authorize the taxing of one person on another person's income; neither does the statute or any section thereof require that such be done. It has been urged that the peculiar wording of the statute, section 218(a) * * * requires that the distributive share of the profits of the partnership shall be taxed to the partners. * * * If the statute be construed so as to tax the husband with that income, when the wife is the owner of the income, a meaning is given to that statute that renders it clearly unconstitutional."

To the same effect is the vigorous dissenting opinion of Judge Manton in *Mitchel v. Bowers*, 15 Fed. (2d) 287, 289-292.

The view so expressed has been adopted and approved by this Court. In *Hoeper v. Tax Commission of Wisconsin*[1] No. 17 decided by this Court on November 30, 1931, this Court condemned the interpretation of a Wisconsin statute which would have taxed husband's and wife's income as a unit. The Court said:

> "Since, then, in law and in fact, the wife's income is in the fullest degree her separate property and in no sense that of her husband, the question presented is whether the State has power by an income tax law to measure his tax, not by his own income but, in part, by that of another."

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[1]Not yet officially reported.

After quoting with approval from *Knowlton v. Moore*, 178 U. S. 41, 77, the Court proceeded:

> "We have no doubt that, because of the fundamental conceptions which underlie our system, any attempt by a State to measure the tax on one person's property or income by reference to the property or income of another is contrary to due process of law as guaranteed by the Fourteenth Amendment. That which is not in fact the taxpayer's income can not be made such by calling it income."

If the Wisconsin statute under consideration by this Court in *Hoeper v. Tax Commission* (*supra*) violated the Fourteenth Amendment, then clearly Section 218(a) of the Revenue Acts would come within the ban of the Fifth Amendment were the construction claimed for it by the Petitioner herein to be adopted. In accordance with well established rules of construction the statute in question should be so construed as to be upheld if possible and any doubts in a taxing statute should be resolved in favor of the taxpayer. (*Reinecke v. Northern Trust Company*, 278 U. S. 339, 348, 349; *Gould v. Gould*, 245 U. S. 151, 153; *United States v. Merriam*, 263 U. S. 179, 187.) This result can be accomplished only by rejecting the construction claimed by the Petitioner herein for Section 218(a); thereby adhering to the conception and definition of income laid down by this Court in *Eisner v. Macomber* and other cases (*supra*).

V.

THE CASES RELIED UPON BY THE COMMISSIONER ARE BASED ON FACTS READILY DISTINGUISHABLE FROM THOSE OF THE INSTANT CASE: THEY APPLY TO ATTEMPTED ASSIGNMENTS OF FUTURE INCOME ONLY (AS DISTINGUISHED FROM AN ASSIGNMENT OF CORPUS AS HEREIN) OR TO REVOCABLE GRANTS (AS DISTINGUISHED FROM AN IRREVOCABLE ASSIGNMENT OF CORPUS AS FOUND HEREIN).

The petitioner, in his "summary of argument," discloses (brief p. 5) that he does not give proper force and effect to the findings of fact herein. For he argues:

> "Although it (Congress) treated partnership income in accordance with the doctrine of the common law, nothing in the statutes indicates that it intended to permit a further reduction by partial *assignments of what a partner might withdraw.* We submit that no agreement or assignment *in respect of the income* of the partnership can relieve a partner from a tax on all of his share of the partnership income * * *."

The authorities cited by counsel support the proposition so stated but they are utterly inapplicable to the instant case, wherein the respondent constituted his wife a half owner of his interest in the business itself. Let us analyze as briefly as possible the cases cited in petitioner's brief.

Mitchel v. Bowers, 15 Fed. (2d) 287, and *Harris v. Commissioner,* 39 Fed. (2d) 546, by the very language quoted at page 9 of petitioner's brief, are directed only against "partial assignments of so much as a partner may withdraw" i.e. against assignments of a share in profits rather than assignments of a share in the business itself. From the findings of fact in the *Mitchel* case (1 B. T. A. 144 and 15 Fed. (2d) pp. 288, 9) it clearly appears that the agreement between Mitchel and his wife contained no language purporting to convey to her a present interest in his interest in the partnership; on the contrary, the agreement

merely provided that the two should share the profits and losses *which he might receive* or to which he might be subjected; and, furthermore, the agreement contained the further important provision (absent in the instant case) that "the contract might be terminated at the option of either party 'at any time'." Judges Hand and Hough, constituting the majority of the court, seized upon this last provision (of revocability) as offering an escape from a difficult "dilemma," saying (p. 289):

> "As to these it may be plausibly argued that, since she could get nothing till the profits should '*come to*' him, and since he was to 'hold for and pay to' her all that he got, the profits must be his before they became hers. On the other hand, since they became hers, at least in equity (*Barnes v. Alexander*, 232 U. S. 117) as soon as he got them, it must be admitted that there was no instant of time after their distribution at which she was not entitled to them. Whatever might be the dialectical escape from the dilemma so raised, it seems to us that in any view the provision which allowed him at his pleasure to denounce the agreement put the absolute disposition of the profits always within his power. * * * It seems to us enough that the plaintiff retained the power to resume his title to the profits when he chose."

The strong dissenting opinion of Judge Manton (pp. 289-292) applies with even greater force to facts such as those herein. And furthermore the first paragraph of the syllabus of the case, which presumably reflects the views of the majority of the Court, indicates clearly that, upon facts comparable to those of the instant case, the decision would have been different:

> "1. In New York contract between husband and wife, entitling wife to *one-half of husband's profits* from partnership, and making wife liable for one-half of losses, assented to by other partners, did not make wife a partner, *since it did not give her any present interest, equitable or legal, in firm assets.*"

In *Harris v. Commissioner*, 39 Fed. (2d) 546, the same Court (Second Circuit) ruled upon the facts there presented, directly and almost solely on the authority of *Mitchel v. Bowers (supra)*. From the opinion (p. 547) it appears that Harris, as distinguished from the respondent herein, had no intent to convey to his wife any interest in the partnership as such, but only "to give a present share to his wife of his interest in the firm *profits.*" From the opinion (p. 547) we quote:

> "A partner who attempts to convey his interest in the profits of the firm, but not in its assets, can therefore do no more than agree that, as soon as he withdraws his share, the assignee shall be at once entitled to them; his assignment has no immediate effect * * *. All this we recognized in *Mitchel v. Bowers*, 15 Fed. (2d) 287, *though our decision primarily rested upon the power reserved to the husband to end the agreement*, which left the disposition of the profits always in his hands."

As indicated by the opinions as well as by the syllabi, *Mitchel v. Bowers* and *Harris v. Commissioner* have application to cases wherein the assignment is of future profits only; moreover, by the very statement of the Court, *Mitchel v. Bowers* was decided as it was "primarily" because of the right of revocation retained by the husband. And furthermore both cases must be read in the light of *Commissioner v. Field*, 42 Fed. (2d) 820, wherein it was recognized by the same court that the rule of *Mitchel v. Bowers* does not apply where a present corpus is assigned and the income in question flows from such assigned corpus. At page 822 the Court said:

> "The Supreme Court has declared in the broadest language that instruments intended to deflect income, subsequently falling due serially, from a husband to his wife are unavailing for tax purposes (*Lucas v. Earl*, 281 U. S. 111, 50 S. Ct. 241, 74 L. Ed. 731), thus tak-

ing a more comprehensive view of the statute than we found necessary in *Mitchel v. Bowers,* (C. C. A.) 15 F. (2d) 287, and *Harris v. Comm'r* (C. C. A.) 39 F. (2) 546. These were, however, all cases in which, though the instrument affected to convey an existing interest in property, there was none at the time which the law recognized. We do not understand that, where there are such, they may not be assigned like other property, or that, when they have been, the income is still taxable to the assignor. Hence the case turns upon whether, after the Illinois decree, Marshall had a present interest in the income of Henry's share assignable under the law of Illinois. If so, his deed as effectively divested him of the assigned interest, as though it had been land or a chattel; his wife became the beneficiary under the trust, and was the only person who could be taxed."

Lucas v. Earl, 281 U. S. 111, is unquestionably a case of outstanding significance. A correct understanding of its import and scope, however, must be predicated upon an analysis of its facts. The Government's claims, as stated by the Court (p. 113) pertained only to "the gain derived from labor", the contention being that such gain "can be salary only to the person who has performed the services": "The purpose of Congress cannot be defeated by an agreement—such as respondent made with his wife—that his earnings, including salaries and fees, *should be received* by him and his wife as joint tenants." That the controversy was so limited in scope is evidenced by the Court's reference to the statute upon which the decision is based (p. 114):

> "The Revenue Act of 1918 * * * Sections 210-212(a) 213(a) * * * imposes a tax upon the net income of every individual, including 'income derived from salaries, wages, or compensation for personal service' ",

making no reference whatever to those portions of the same sections which include in the definition gains from other sources, such as those springing from invested capital. The Court held the quoted portion of the law effective to "tax salaries to those who earned them" concluding with the words (p. 115):—

> "That seems to us the import of the statute before us and we think that no distinction can be taken according to the motives leading to the arrangement by which the fruits are attributed to a different tree from that on which they grew."

Lucas v. Earl, by its very language, obviously lays down no rule as to tax incidence concerning income which flows from assigned corpus such as a partnership interest rather than from personal service. This Court indicated by its closing words in that case that the true test is: "On what tree did the fruit grow?" And so, in *Poe v. Seaborn,* 282 U. S. 101, 117, this Court defined the scope and effect of *Lucas v. Earl,* saying:

> "We held that assuming the validity of the contract under local law, it still remained true that the husband's professional fees, earned in years subsequent to the date of the contract, were his individual income, 'derived from salaries, wages, or compensation for personal services', under Sections 210, 211, 212(a) and 213 of the Revenue Act of 1918. The very assignment in that case was bottomed on the fact that the earnings would be the husband's property, else there would have been nothing on which it could operate."

Larsen v. Burnet, 50 F. (2d) 308 (Ct. App. D. C.) is relied upon by the petitioner. From the facts of that case as reported at 14 B. T. A. 163 it appears that the husband and wife entered into no agreement whatsoever; the husband, a member of a partnership, had utilized certain property which had been "community property" in another

state as his capital contribution to the firm, erroneously assuming (according to the court) that the wife would be entitled to one-half of the profits on the theory that she remained the equitable owner of a moiety of the property which he had invested. The Court ruled that the husband alone was a partner and that he alone was taxable on his share of the profits. Concerning this case it may be said, first, it seems in direct conflict with *Rucker v. Blair,* (C. C. A. 9th *infra*) which was approved and followed in *Poe v. Seaborn (infra),* and secondly, it must be read in conjunction with *Hall v. Burnet* decided by the same court (Ct. App. D. C.) *(infra).*

In citing and relying upon *Hill v. Commissioner,* 38 F. (2d) 165, *Pope v. Commissioner,* 39 F. (2d) 420, 424 and *Benedict v. Collector,* 38 F. (2d) 309, 313-314, the petitioner has, we submit, gone far afield. These cases involved substantially the same facts, not at all comparable to the issue which is involved in the case at bar. The *Hill* case is typical of the three. The facts were that one of the members of a partnership had died and the surviving partners, in accord with the terms of the partnership agreement, paid to the estate of the deceased partner over a period of years "*sums equal to* the full amount of the net profits which he would have received had he lived and the business had gone on." (168) The Court in each case properly held upon such facts that the surviving partners, constituting a new partnership from and after the death of the deceased partner, were chargeable with all of the net income of the new partnership without deduction of amounts paid to the estate of the deceased partner, which payments were for "the purchase of a capital asset" to-wit, the interest of the former partner. In the *Hill* case the Court said (at p. 168):

> "Those payments could be made out of any funds from which the petitioners chose to make them • • •

> the mere fact that the petitioners * * * elected to have it (the obligation) discharged out of the undistributed profits of the new firm did not create a charge upon those profits, nor diminish the petitioners' distributive shares therein. * * * The old firm was dissolved by S's death and his interest passed to the petitioners, subject to the payments they were to make under Article 14 * * * the payments * * * were made by the petitioners in the purchase of a capital asset."

Concerning the Board cases cited at p. 14 of petitioner's brief we may say: *Appeal of Mitchel*, 1 B. T. A. 143, 148, is the same case as *Mitchel v. Bowers* already discussed; *Appeal of Kneeland*, 1 B. T. A. 150, involved the same firm and the same facts as the *Mitchel* case; *Levering v. Commissioner*, 5 B. T. A. 616, involved an assignment of prospective profits only; so also *Knapp v. Commissioner*, 5 B. T. A. 762, *King v. Commissioner*, 10 B. T. A. 698, *Colbert v. Commissioner*, 12 B. T. A. 565 and *Staebler v. Commissioner*, 17 B. T. A. 1086. The *Luce* case, (18 B. T. A. 923) involved an attempt by a firm of lawyers to accomplish the identical thing which was denounced in *Lucas v. Earl (supra)*. The *Battleson* case, (22 B. T. A. 455) was so close upon its facts that strong dissenting opinions were written and concurred in by five members of the Board. The *Cohan* case, 11 B. T. A. 743 (a companion case to the *Harris* case which we have already discussed) went to the Circuit Court of Appeals (39 F. 2d, p. 540) which affirmed the Board in part, saying at p. 542:

> "There can be no doubt that he remained always free to stop his payments, and that her share depended on the endurance of his feelings toward her."

In other words the Court in the *Cohan* case found a situation exactly analogous to that in *Mitchel v. Bowers, supra*, so that the entire income from that source was taxable to Cohan. However, at page 543, the Court had for consideration other sources of income involving ownership

of the corpus by a transferee and with reference thereto modified the decision of the Board, holding that the tax incidence was upon the owner of the corpus from which the income flowed.

The petitioner challenges our reliance upon the Board cases of *Wing v. Commissioner*, 17 B. T. A. 1028, and *Dickinson v. Commissioner*, 23 B. T. A. 1211. But these cases are of the utmost significance because, under the law of Michigan therein involved, partnerships between husband and wife were forbidden. How can the petitioner reconcile his contention that only the record partners in a partnership (and not the equitable owners of the partnership shares) may be taxed on partnership income with the conclusion of the Board in the *Wing* case

> "That, the beneficial ownership of a one-sixth interest in the partnership property being in petitioner's wife [1] one-sixth of the earnings of the partnership represented income to her and not to petitioner"?

The entire contention of the government in the instant case was answered by the Board in the *Wing* case (at p. 1030) in these words:

> "In this theory it has been overlooked that the identity of the party taxable upon income from a partnership interest is not determined merely by the name in which such interest is held but by the ownership of the corpus of the partnership interest."

The petitioner next discusses "three analogous situations where one who is not the ultimate beneficial owner of income is taxed upon it." It should be observed that we contend for the taxability of the income to the respondent's wife rather than to the respondent not alone because of her beneficial ownership of the income as such, but also, and more fundamentally, because of her beneficial ownership of the corpus from which that income flowed.

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[1] Who under the law, could not be a partner.

However, considering the three categories suggested by petitioner's argument:—

(1) *Lucas v. Earl* is cited as typical of cases in the first category. In that case this Court said (at p. 115):

> "There is no doubt that the statute could tax salaries to those who earned them and provide that the tax could not be escaped by anticipatory arrangements * * * devised to prevent the salary when paid from vesting even for a second in the man who earned it."

But partners, in the absence of special agreement, do not receive salaries or compensation for services as such (*Parsons on Partnership*, 4th Ed., §155). What they receive is a share of the partnership profits and (we believe) the Commissioner has always treated income from a partnership in this manner, denying a partnership deductions for salaries of partners.

The form provided by the Commissioner of Internal Revenue for the return of partnership income contains an "instruction" reading as follows:

> "Enter as Item 13 all salaries and wages not included as a deduction in Line C of Item 2, *except compensation for partners, which shall not be claimed as a deduction in this item or elsewhere on the return.*"

The Respondent had no right to determine the deductions from gross income as suggested by the quotation at page 23 of Petitioner's brief; these deductions are definitely prescribed by law. Furthermore, as to the argument (petitioner's brief, pp. 18, 19) that amounts received by the Respondent must be treated as compensation for services, such suggestion does not conform with law. In G. C. M. 6582; CB Dec. 1929, page 200, the opinion of the General Counsel of the Bureau of Internal Revenue contains the following:

> "* * * *for income tax purposes so-called salaries of partners can not be recognized and are not permitted*

> *as deductible operating expenses of a partnership,* for the reason that partners receiving from partnership funds any sums of money necessarily receive such sums either out of the profits made by the partnership or, if there be no sufficient profit made, then out of the capital investment. Partners are working for themselves, and, in contemplation of law, a man may not constitute himself his own employee. (*Estate of S. U. Tilton et al. v. Commissioner,* 8 B. T. A., 914 (C. B. June 1928, p. 31)); appeal of *Harriet Taylor,* 2 B. T. A., 1159 (C. B. June 1928, p. 31.) Therefore, whatever is received by a partner in the form of or under the name of salary constitutes nothing more or less than a withdrawal from the partnership of anticipated profits, * * *."

See also *In re Karl Pauli,* 11 B. T. A. 784. The last mentioned case and also the cases cited in the General Counsel's Memorandum were acquiesced in by the Commissioner.

But, what is more fatal to the argument, every assignment of the kind condemned in *Lucas v. Earl* and kindred cases, is subject to the infirmity pointed out by this Court in *Poe v. Seaborn,* 282 U. S. 101 at p. 117, as follows:

> "The very assignment in that case was bottomed on the fact that the earnings would be the husband's property, else there would have been nothing on which it could operate."

In other words, these cases involve not the assignment of an existing income-producing corpus; but rather, and solely, the transfer of income arising in the future *qua* income, such income being the property of the assignor *when earned and received* and therefore taxable to him.

(2) The cases which come within the rule of *Bing v. Bowers* have already been fully discussed in this brief. They were all cases (as said in *Copland v. Commissioner, supra*) involving transfers "without consideration (of) a thing not in existence." And furthermore they were predicated upon mere assignments of future income. The dis-

tinction between such cases and the instant one is well stated in one of the cases which counsel now cite, *Bishop v. Commissioner,* No. 4517, decided by the Circuit Court of Appeals (7th) on December 9th, 1931, wherein the court said:

> "The distinction is very clearly recognized in *Hall v. Burnet, Commissioner,* No. 5173, decided by the Court of Appeals of the District of Columbia, November 16, 1931, but not yet published. In that case appellant, a life insurance agent, entered into a contract with his second wife, in which her rights in his property were defined for the protection of his children by a former marriage, in consideration of which she renounced her dower. Among other considerations moving from him he sold, assigned, and transferred to her an undivided interest in his *contract* with the insurance company. The court held that one-half of the subsequent renewal commissions should be taxed not to appellant but to the wife, as income accruing to her from the property right which appellant had assigned to her. The court said:
>
> "'* * * It is obvious that if what was here sought to be conveyed from the husband to the wife was salary, or personal earnings, the same would still be taxable to him though he never actually received it, but in the view we take of the case, what was assigned was neither income nor earnings, but property. It was not an assignment of future earnings but the transfer of a property right, and though this property right gave rise to future income, uncertain and contingent though it might be as to amount, that fact does not destroy the distinction.' "

See also

Copland v. Commissioner, C. C. A. 7th, *supra;*
Commissioner v. Field, C. C. A. 2nd, *supra;*
Kaufman v. Commissioner, 44 F. (2) 144, C. C. A. 3rd;
O'Malley-Keyes v. Collector, 24 F. (2) 436;

Young v. Collector, 28 F. (2) 789;
McKee v. Collector, 48 F. (2) 838.

(3) *Corliss v. Bowers*, 281 U. S. 376, which petitioner cites in his third category of cases wherein income beneficially belonging to one was taxed to another seems far afield. The court held:

> "The grantor of a *revocable* trust may constitutionally be assessed for income tax in respect of income from the trust fund, though such income was actually paid to the beneficiary, and so passed beyond his power to appropriate."

In the opinion (p. 378) the court said:

> "The acquisition by the wife of the income became complete only when the plaintiff failed to exercise the power that he reserved. *Saltonstall v. Saltonstall*, 276 U. S. 260; *Chase Nat. Bank v. United States*, 278 U. S. 327; *Reinecke v. Northern Trust Co.*, 278 U. S. 339.
>
> "Still speaking of taxation, if a man disposes of a fund in such a way that another is allowed to enjoy the income which it is in the power of the first to appropriate, it does not matter whether the permission is given by assent or by failure to express dissent. The income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his own income, whether he sees fit to enjoy it or not."

Such words, applicable to the facts of *Corliss v. Bowers, Mitchel v. Bowers* and other cases cited by petitioner in this group, can have no application to the instant case wherein not only the income, but a half interest in the corpus which produced it as well, had irrevocably passed beyond the respondent's control.

We submit that the distinction between such cases and the instant case is analogous to that existing between cases (involving the estates tax) as *Chase National Bank v.*

United States, 278 U. S. 327, on the one hand, and *May v. Heiner*, 281 U. S. 238, *Burnet v. Northern Trust Company*, *Morsman v. Burnet*, and *McCormick v. Burnet*, 283 U. S. 782-785, on the other; the former involving retention of control by the grantor as in *Mitchel v. Bowers*, and the latter group involving complete and irrevocable passage of title *in praesenti* as in the case at bar. And so in *Reinecke v. Northern Trust Company*, 278 U. S. 339, this Court held one group of trusts to have been within the control of the settlor and therefore taxable, while holding another group of trusts non-taxable as having been completely irrevocable by the settlor from the date of their creation. The words used by this Court in *Chase National Bank v. United States*, 278 U. S. at page 336, apply to the facts of *Mitchel v. Bowers* and *Corliss v. Bowers* (*supra*) but have no application to the facts of the instant case:

> "Such an outstanding power reserved exclusively in a donor to recall a gift after it is made is a limitation on the gift which makes it incomplete as to the donor as well as to the donee * * *."

On the contrary the rule and language of *May v. Heiner* (*supra*, at p. 243) apply here in that the transfer from respondent to his wife of the income-producing corpus was complete and "beyond recall."

The so-called *Community Income Tax* cases decided by this Court November 24, 1930, are of outstanding significance because of the similarity between Community and Partnership title. *McKay on "Community Property,"* 2nd Edition, stresses this similarity (see pp. 113, 121, 762, 823). At p. 823 for example the learned author says:

> "Even though we may deny that express or implied contract is the actual basis of the legal community we are forced to admit that the wife's rights are the same in kind as though she had entered into a contract with her husband making the provisions of

law regulating the legal community the terms of this contract."

Wherever community property rights exist the analogy between community and partnership title is asserted. The points of distinction are technical and not material to our present deliberation (*Holyoke v. Jackson*, 3 Wash. T. 235; *Weil v. Jacobs*, 111 La. 357; *Gulf R. R. Co. v. Goldman*, 87 Tex. 567). In *Cervantes v. Cervantes*, 76 S. W. 790, 792, the Texas court said:

> "The laws of Texas create a partnership between the husband and wife, and declare that all property acquired during the existence of the partnership, as in other partnerships, shall be a common fund, except that derived from sources independent of and disconnected with the partnership."

Poe v. Seaborn, 282 U. S. 101, as decided by this Court, affirmed the same case as decided by the Circuit Court of Appeals (9th) which, in turn, had affirmed the District Court's decision reported in 32 Fed. (2d) 916. A reading of the last mentioned decision discloses that the District Court had based its conclusions squarely on *Rucker v. Blair*, 32 Fed. 2, p. 222. In that case the Circuit Court of Appeals (9th) had held that husband and wife might properly each return one-half of the income accruing upon an interest in a partnership which had been acquired with community funds. The court said (at p. 223):

> "The partnership return for 1918 exhibited a total distributive income of $95,699.27 divided equally between the two partners. Petitioner * * * made his individual tax return for one-half only of his distributive share, upon the assumption that it was community income, and that therefore the other half was returnable by his wife * * * (p. 224). The mere fact that the enterprise was carried on in the firm name is immaterial. There is no alchemy in the term 'partnership' or in the relation it imports, and contributions of community funds to a joint or partnership enterprise are not

ipso facto converted into separate property. We are concerned with *the status of property invested*, not with the form in which it was held."

In *Poe v. Seaborn* this Court (at p. 109) reasoned that the applicable sections of the several Revenue Acts levied a tax on the income "of" every individual; that the word "of" was intended to denote "ownership"; that under the laws of Washington "the wife has a vested property right in the community property equal with that of her husband" (p. 111); that the income attributable to her community interest is hers, not his, notwithstanding the broad powers of management and disposition which the law gave him. The court said (at p. 112):

> "The same policy dictates that third parties who deal with the husband respecting community property shall be assured that the wife shall not be permitted to nullify his transactions. The powers of *partners*, or of trustees of a spendthrift trust, furnish *apt analogies*. * * * (p. 113). The law's investiture of the husband with broad powers by no means negatives the wife's present interest as a co-owner."

In *Goodell v. Koch*, 282 U. S. 118, 121, this Court said:

> "The Arizona Supreme Court has *likened the community to a partnership. Forsythe v. Paschal*, 34 Ariz. 380, 271 Pac. 865. The husband as agent may not act in fraud of his wife's rights, and if he attempts to do so, she has a remedy in the courts. *Gristy v. Hudgens*, 23 Ariz. 339, 203 Pac. 569."

In *Hopkins v. Bacon*, 282 U. S. 122, 125, 126, the Court used these words:

> "'In view of our decision in No. 15 (*Poe v. Seaborn, supra*), the only matter to be examined here is whether under the community property system of Texas the wife has a mere expectancy, as she would under the law of California (Cf. *United States v. Robbins*, 269 U. S. 315) or, on the contrary, has a proprietary vested

interest in the community property such as makes her an owner of one-half of the community income.

"In view of what has been said in No. 15, it remains only to say that the interest of a wife in community property in Texas is properly characterized as a present vested interest, equal and equivalent to that of her husband, and that one-half of the community income is therefore income of the wife. She and her husband are entitled to make separate returns, each of one-half of such income."

In *Bender v. Pfaff*, 282 U. S. 127, the Court held to the same effect and, in the course of the opinion said (131, 132):—

"Repeatedly the statutes refer to the relation as a 'partnership or community' * * *. Inasmuch, therefore, as in Louisiana, the wife has a present vested interest in community property equal to that of her husband, we hold that the spouses are entitled to file separate returns, each treating one half of the community income as income 'of' each of them as an 'individual' as those words are used in Sections 210(a) and 211(a) of the Revenue Act of 1926."

Poe v. Seaborn (*supra*) and the other "Community Income Tax cases" decided by this Court November 24, 1930 were distinguished by this Court from *United States v. Robbins*, 269 U. S. 315, on the ground that under the California law involved in the *Robbins* case the wife had

"a mere expectancy and * * * the property rights of the husband during the life of the community were so complete that he was in fact the owner." (282 U. S. 116)

Subsequent to the decision in the *Robbins* case the California law was amended in such manner as to constitute the wife's community interest a vested estate rather than a mere expectancy and this Court in *United States v. Malcolm*, 282 U. S. 792, answered questions certified to it and arising under the amended California law in harmony

with its decisions in *Poe v. Seaborn* and the other community cases (*supra*).

The distinction so drawn by this Court between "a mere expectancy" and "a present vested interest" applies with like force to cases such as *Mitchel v. Bowers* on the one hand and the case at bar on the other; in the former the thing assigned was a "mere expectancy"; in the instant case it was "a present vested interest" in an existing corpus. The income involved herein was, in the words of *Lucas v. Earl* (*supra*) "fruit" which grew upon a "tree" of which the respondent's wife was the owner and the income was taxable to her, not to the respondent.

CONCLUSION.

We strongly suspect that this case would never have been presented to this Court were it not that the opinion of the court below contains a remote challenge to the validity of *Mitchel v. Bowers*. That challenge, if it be such, because of the disparity between the facts of that case and this, was quite unnecessary to the decision reached by the Circuit Court of Appeals.

> "It is judgments, decrees and rulings which an appellate court reviews and not opinions or reasons, and if the judgment, decree or ruling is correct, the court will not inquire into the reasons assigned * * * therefor * * *."
>
> *Cyc. of Federal Procedure*, Vol. VI, page 566, and cases there cited.

We respectfully and earnestly submit that the decision of the court below responds to, and is required by, the facts as found and that, therefore, it should be affirmed.

IRWIN N. LOESER,
Counsel for Respondent.

LEVI COOKE,
GEORGE R. BENEMAN,
Of Counsel.

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FEB 8
CHARLES ELMORE

In the Supreme Court of the United States

OCTOBER TERM, 1931.

No. 426.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

CHARLES P. LEININGER.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

SUPPLEMENTAL BRIEF FOR RESPONDENT.

IRWIN N. LOESER,
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THE GATES LEGAL PUBLISHING CO., CLEVELAND, O.

In the Supreme Court of the United States

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No. 426.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
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CHARLES P. LEININGER.

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SUPPLEMENTAL BRIEF FOR RESPONDENT.

Due to necessary haste in the preparation of respondent's brief the following statement was omitted from Part I thereof at p. 13.

The Petitioner, at pp. 10-11 of his brief, suggests an administrative difficulty in the application of our theory of the case and the decision of the court below, in that the respondent would, under section 218 of the law, be taxable on his share of the net income of the laundry company whether distributed or not, whereas if the income were distributed in the year when earned it would be taxed one-half to respondent and one-half to his wife. But this statement of the petitioner does not correctly interpret either the position of the respondent or the decision of the court below. As we have said, the respondent's wife (as to her share) would stand precisely in the shoes of the respondent. This would be so because, under the findings of fact, she was either

(a) A partner in the laundry company and therefore taxable under section 218 upon her share, whether distributed or not; or

(b) A partner in her husband's interest in an existing corpus and therefore taxable (likewise under section 218) upon the net income thereof whether distributed or not; or

(c) The Beneficiary of an irrevocable trust of which the respondent was the Trustee, in which event section 219 of the act would apply. That section provided:—

> "Sec. 219. (a) That the tax imposed by sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including—
>
> (4) Income which is to be distributed to the beneficiaries periodically, whether or not at regular intervals, * * * and in cases under paragraph (4) of subdivision (a) of this section the fiduciary shall include in the return a statement of each beneficiary's distributive share of such net income, whether or not distributed before the close of the taxable year for which the return is made.
>
> (d) In cases under paragraph (4) of subdivision (a) * * * *the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary his distributive share, whether distributed or not*, of the net income of the estate or trust for the taxable year * * *."

A beneficiary of such an irrevocable trust, being treated under section 219 exactly as a partner under section 218, i.e., taxable on his or her share of net income whether distributed or not, no difficulty of the kind suggested by counsel could arise.

On the other hand, a very serious difficulty arises if we adopt the petitioner's position. For in that event the

respondent would be taxed under section 218 upon one-half of the net income of the laundry company, whether distributed or not, and his wife (either as a partner in his interest under section 218 or as beneficiary of a trust under section 219) would be taxed on her one-half of the respondent's share. For the income distributable to her was not a gift exempt from tax as such; her distributive share was predicated upon a contract supported by a legal consideration and, therefore, taxable to her. The same income, therefore, under the petitioner's theory would be taxed twice, a result scarcely to be tolerated where the things done and the applicable sections of the statute reasonably support the more equitable result of taxing the same income only once and then only to the equitable owner of the corpus from which it flowed.

Respectfully submitted,

IRWIN N. LOESER,

Counsel for Respondent.

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APR 6

In the Supreme Court of the United States

OCTOBER TERM, 1931.

No. 426.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

CHARLES P. LEININGER,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

PETITION OF RESPONDENT FOR REHEARING.

IRWIN N. LOESER,
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THE GATES LEGAL PUBLISHING CO., CLEVELAND, O.

In the Supreme Court of the United States

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IRWIN N. LOESER,
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In the Supreme Court of the United States

OCTOBER TERM, 1931.

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DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

CHARLES P. LEININGER,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.

PETITION OF RESPONDENT FOR REHEARING.

To the Honorable Justices of the Supreme Court of the United States:

Comes now Charles P. Leininger, the respondent in the above-entitled cause, and presents this, his petition for a rehearing herein upon the following grounds:

1. The case involves a vitally important constitutional question, namely, whether, in the face of the Fifth Amendment, one person may be taxed upon income equitably owned by another. The decision of the Court, we humbly submit, answers this question in the affirmative and thereby sets a precedent, the full import of which this Honorable Court may desire to reconsider. The Court has held "as conclusive" the finding that Mrs. Leininger was "a full equal partner" with her husband in the latter's *interest* in the partnership. The Court limits the effect of this unchallenged finding by holding that it "cannot be taken to have amounted to more than *an equitable assignment* of one-half of what her husband should receive from the part-

nership." The Court refers to the argument "that the statute seeks to tax only income beneficially received" but concludes, upon a close reading of the precise words of Section 218(a) of the Revenue Act of 1918, that it requires a tax upon Partner A measured by his full *record* share of the profits, even though another, not a partner in the principal venture, is the owner of a portion of his "*interest.*" We present for the further patient and indulgent consideration of the Court the question whether the decision herein does not so construe and apply Section 218(a) as to result in the taking of the property of A without due process, in violation of the Fifth Amendment.

2. Section 218(a) of the Revenue Act of 1918, not heretofore construed by this Honorable Court, should be construed as being *in pari materia* with certain other sections of the Act and harmoniously therewith. Not only is it true "that the statute *seeks* to tax only income beneficially received," but that plan of the statute is specifically and expressly ordered by portions of Sections 200, 219, 224 of the same Act. These, so far as here material, appear in the appendix hereof. These sections, when read in conjunction with Section 218(a), definitely require that even as to partnership interests, the equitable owner, rather than the nominal primary recipient, must bear the tax burden. Section 224 by its very words distinguishes between the "individuals * * * entitled to share in the net income" and "partners." These words used in Section 224 indicate clearly that Congress contemplated that "individuals" other than "partners" might be entitled to receive the income of a partnership and that they, rather than the partners as such, would be subject to the tax thereon.

3. With respectful deference to the Court, we submit that its decision does not give due effect to the unchallenged finding that the respondent's wife was a full equal

partner with him in his *interest* in the partnership. We submit that she was the owner *pro tanto,* not alone of her portion of the profits, but also of a partnership "interest" of the same quality and with the same incidents (save only the right to participate in business control) as appertained to that interest as owned by the respondent prior to its subdivision with her. Can it be said that a partner's interest is a right merely to share in profits? It must be more than that; it embraces an equitable ownership of the partnership capital subject to claims of creditors; a partner's interest has repeatedly been defined and recognized as an assignable property right. However we may define it, that interest in its totality of import was equitably owned in part by the respondent's wife. A share in the partnership interest was hers; her participation in the profits was not by reason of an assignment of profits arising *in futuro* as in *Lucas v. Earl. It was an incident of her part ownership of the partnership interest.* The share of profits was hers *before* and *not after* it accrued to him; her share, in fact and law, *never* accrued to him beneficially and should not be taxed to him. The test of *Lucas v. Earl,* we humbly submit, should result in affirmance rather than reversal of the Court below, for the "fruit" grew on a tree of which she was the owner.

With full submission, counsel humbly state that they believe the problem presented is of such importance as to warrant further consideration by this Honorable Court, and, therefore, respectfully pray that a rehearing may be ordered herein.

Respectfully submitted,

IRWIN N. LOESER,
Counsel for Respondent,
National City Bank Building,
Cleveland, Ohio.

CERTIFICATE OF COUNSEL.

I, counsel for the above-named Charles P. Leininger, respondent, do hereby certify that the foregoing petition for a rehearing of this cause is presented in good faith and not for delay.

IRWIN N. LOESER,
Counsel for Respondent.

APPENDIX.
REVENUE ACT OF 1918.

Sec. 200. That when used in this title—
The term "fiduciary" means * * * any person acting in any fiduciary capacity for any person, trust or estate;

Sec. 219 (a). That the tax imposed by Sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including—

(4) Income which is to be distributed to the beneficaries periodically, whether or not at regular intervals, * * * (b) * * *; and in cases under paragraph (4) of subdivision (a) of this Section the fiduciary shall include in the return a statement of each beneficiary's distributive share * * * (d) In cases under paragraph (4) of subdivision (a) * * * the tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary his distributive share, whether distributed or not, of the net income of the estate or trust for the taxable year. * * *

Sec. 224. That every partnership shall make a return for each taxable year * * * and shall include in the return the names * * * of the *individuals* who would be entitled to share in the net income * * * and the amount of the distributive share of each *individual*. The return shall be sworn to by any one of the *partners*.

Sec. 225. Fiduciaries required to make returns under this Act shall be subject to all the provisions of this Act which apply to *individuals*.

SUPREME COURT OF THE UNITED STATES.

No. 426.—October Term, 1931.

David Burnet, Commissioner of Internal Revenue, Petitioner, *vs.* Charles P. Leininger. | On Writ of Certiorari to the United States Circuit Court of Appeals for the Sixth Circuit.

[March 14, 1932.]

Mr. Chief Justice Hughes delivered the opinion of the Court.

The respondent sought a redetermination of deficiencies in income taxes for the years 1920 to 1923. The question related to the income earned on respondent's share in a partnership known as the Eagle Laundry Company, doing business in Cleveland, Ohio. By virtue of an agreement made with his wife, respondent insisted that she was 'a full equal partner with him in his interest in the partnership', and that each should return and pay tax upon one-half of the income attributable to that interest. The Commissioner determined that respondent was taxable upon the whole of the income earned on his share in the partnership and the Board of Tax Appeals affirmed that decision. 19 B. T. A. 621. The Circuit Court of Appeals reversed the order of the Board (51 Fed. (2d) 7), and this Court granted a writ of certiorari.

The question arises under Section 218 (a) of the Revenue Acts of 1918 and 1921 (40 Stat. 1070; 42 Stat. 245) which provided:

"That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year . . ."

There is no challenge to the findings of fact made by the Board of Tax Appeals as being unsupported by evidence, and they must be treated as conclusive. *Phillips* v. *Commissioner*, 283 U. S. 589, 599, 600. Upon these findings, which are set forth in the margin,[1] it cannot be maintained that the agreement between the respondent and his wife made her a member of the partnership. That re-

[1]The findings of the Board of Tax Appeals are as follows:

"In 1898 a partnership known as Eagle Laundry Company was organized by petitioner and one M. G. Monaghan, each owning a one-half interest. In 1904 Monaghan died and his wife, Mary T. Monaghan, succeeded to his in-

sult could not be achieved without the consent of the other partner or partners,[2] and there is no finding of such consent. The mere communication of the fact that the agreement had been made was not enough. It does not appear that there was any attempt to change the ownership of the partnership assets or the control of the partnership enterprise. It was the husband's interest that was the subject of the agreement.[3] His wife was to be an 'equal partner with him' in that interest. The business of the firm was

terest in the firm and on the books of the company. In 1920 Mary T. Monaghan transferred by bill of sale her interest to her children. The entire Monaghan interest was thereafter carried on the books in the name of Marcus A. Monaghan. The partnership returns for the years 1921, 1922 and 1923 filed by Eagle Laundry Company disclose the partners to be petitioner and M. T. Monaghan and the income to be distributable one-half to each. Each of the three children of Mary T. Monaghan, however, returned a proportionate part of the income for taxation.

"During the latter part of 1920 a written agreement confirmatory of a pre-existing oral agreement, was entered into between petitioner and his wife, wherein it was acknowledged that petitioner's wife had been and was a full equal partner with him in the interest in the Eagle Laundry Company, entitled to share equally in the profits and obligated to bear equally any losses. The contract was effective from the beginning of 1920. The written agreement was not produced, probably having been lost in a fire at the plant. The fact of this transfer was communicated to Marcus A. Monaghan, who represented the owners of the other one-half interest in the Eagle Laundry Company. The Leininger interest always stood in the name of C. P. Leininger on the partnership books but Mrs. C. P. Leininger returned one-half of the profits of the Leininger interest for taxation.

"Petitioner and his wife maintained prior to and throughout the period here involved a joint bank account on which each could draw unrestrictedly. The profits received from the partnership were deposited in this account by Leininger, no checks on the partnership being drawn to the wife. After the execution of the agreement the wife also maintained a small personal account in which were deposited checks received on account of earnings on her personal investments. Mrs. Leininger took no part in the management of the business and made no contribution to its capital. There was never any formal accounting between petitioner and his wife."

[2] Channel *v.* Fassitt, 16 Ohio 166; Pagel *v.* Creasy, 6 Ohio App. 199, 207, 208; McNamara *v.* Gaylord, 3 Ohio Fed. Dec. 543, 546, 1 Bond 302; Bank *v.* Carrollton Railroad, 11 Wall. 624, 628, 629; Burnett *v.* Snyder, 76 N. Y. 344, 349; Cohan *v.* Commissioner, 39 Fed. (2d) 540, 542.

[3] See Nixon *v.* Nash, 12 Ohio St. 647, 650; Bank *v.* Carrollton Railroad, *supra;* Case *v.* Beauregard, 99 U. S. 119, 124; Burnett *v.* Snyder, *supra;* Rockafellow *v.* Miller, 107 U. S. 507, 510; Mitchel *v.* Bowers, 15 Fed. (2d) 287, 288; Cohan *v.* Commissioner, *supra;* Harris *v.* Commissioner, 39 Fed. (2d) 546, 547.

continued as before. Complying with the statute,[4] the partnership returns, verified by the husband for the years in question, stated that the names of the partners were 'C. P. Leininger and M. T. Monaghan, each owning one-half.' 19 B. T. A. at p. 623. The 'Leininger interest' remained in the name of the respondent on the partnership books. His wife took no part in the management of the business and made no contribution to its capital. The profits received from the partnership went to the respondent, no checks on the firm being drawn to the wife. Upon the facts as found, the agreement with Mrs. Leininger cannot be taken to have amounted to more than an equitable assignment of one-half of what her husband should receive from the partnership, she in turn agreeing to make good to him one-half of the losses he might sustain by reason of his membership in the firm.

The respondent urges that the assignment to his wife was of one-half of the *'corpus'* of his interest and that this *'corpus'* produced the income in question. The characterization does not aid the contention. That which produced the income was not Mr. Leininger's individual interest in the firm, but the firm enterprise itself, that is, the capital of the firm and the labor and skill of its members employed in combination through the partnership relation in the conduct of the partnership business. There was no transfer of the *corpus* of the partnership property to a new firm with a consequent readjustment of rights in that property and management. If it be assumed that Mrs. Leininger became the beneficial owner of one-half of the income which her husband received from the firm enterprise, it is still true that he, and not she, was the member of the firm and that she had only a derivative interest.

The statute dealt explicitly with the liability of partners as such. Applying to this case, the statute provided that there should be included in computing the net income of Leininger his distributive share of the net income of the partnership. That distributive share, as he himself stated in his return on behalf of the partner-

[4]Section 224 of the Revenue Acts of 1918 and 1921 (40 Stat. 1074, 42 Stat. 250) provided:

"That every partnership shall make a return for each taxable year, stating specifically the items of its gross income and the deductions allowed by this title, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners."

ship, was one-half. In view of the clear provision of the statute, it cannot be said that Leininger was required to pay tax upon only a part of this distributive share because of the assignment to his wife. The case of *Lucas* v. *Earl,* 281 U. S. 111, is analogous. There the husband made a contract with his wife by which his salary and fees were to be "received, held, taken and owned" by them as joint tenants. The Court recognized that a forcible argument was presented "to the effect that the statute seeks to tax only income beneficially received, and that taking the question more technically the salary and fees became the joint property of Earl and his wife on the very first instant in which they were received". But the case was deemed to turn on the import and reasonable construction of the taxing act. "There is no doubt" said the Court, "that the statute could tax salaries to those who earned them and provide that the tax could not be escaped by anticipatory arrangements and contracts however skilfully devised to prevent the salary when paid from vesting even for a second in the man who earned it. That seems to us the import of the statute before us and we think that no distinction can be taken according to the motives leading to the arrangement by which the fruits are attributed to a different tree from that on which they grew." *Id.,* pp. 114, 115. This ruling was not disturbed by *Poe* v. *Seaborn,* 282 U. S. 101, which pointed out the distinction. *Id.,* p. 117.

We find no reason to doubt the validity of the tax. The Congress, having the authority to tax the net income of partnerships, could impose the liability upon the partnership directly, as it did under the Revenue Act of 1917 (40 Stat. 300, 303), or upon the 'individuals carrying on business in partnership', as in the statutes here involved. The Congress could thus tax the distributive share of each partner as such, as in *Lucas* v. *Earl, supra,* it taxed the salary and fees of the person who earned them. A different situation was presented in *Hoeper* v. *Tax Commission of Wisconsin* (decided November 30, 1931), where the question related to the earnings of the wife and the income which she received from her separate estate. For that which thus belonged to her the Court held that her husband could not be taxed. In the instant case, the right of the wife was derived from the agreement with her husband and rested upon the distributive share which he had, and continued to have, as a member of the partnership.

The decree of the Circuit Court of Appeals is reversed and the order of the Board of Tax Appeals affirmed.

It is so ordered.